No. 17-1077	
Title:	Francis V. Lorenzo, Petitioner v. Securities and Exchange Commission
Docketed:	January 31, 2018
Linked with 17A857	
Lower Ct:	United States Court of Appeals for the District of Columbia Circuit
Case Numbers:	(15-1202)
Decision Date:	September 29, 2017
Questions Presented	

DATE	PROCEEDINGS AND ORDERS
Dec 15 2017	Application (17A857) to extend the time to file a petition for a writ of certiorari from December 28, 2017 to January 26, 2018, submitted to The Chief Justice. Main Document Main Document
Dec 19 2017	Application (17A857) granted by The Chief Justice extending the time to file until January 26, 2018.
Jan 26 2018	Petition for a writ of certiorari filed. (Response due March 2, 2018) Petition Appendix Certificate of Word Count Proof of Service
Feb 23 2018	Motion to extend the time to file a response from March 2, 2018 to April 2, 2018, submitted to The Clerk. Main Document
Feb 27 2018	Motion to extend the time to file a response is granted and the time is extended to and including April 2, 2018.
Mar 26 2018	Motion to extend the time to file a response from April 2, 2018 to May 2, 2018, submitted to The Clerk. Main Document
Mar 28 2018	Motion to extend the time to file a response is granted and the time is further extended to and including May 2, 2018.
May 02 2018	Brief of respondent Securities and Exchange Commission in opposition filed. Proof of Service Main Document

May 22 2018	DISTRIBUTED for Conference of 6/7/2018.
May 23 2018	Reply of petitioner Francis V. Lorenzo filed. (Distributed) **Main Document** **Certificate of Word Count** **Proof of Service**
Jun 11 2018	DISTRIBUTED for Conference of 6/14/2018.
Jun 18 2018	Petition GRANTED.
Jul 31 2018	Motion to extend the time to file the opening briefs on the merits granted. The time to file the joint appendix and petitioner's brief on the merits is extended to and including August 20, 2018. The time to file respondent's brief on the merits is extended to and including October 5, 2018.
Jul 31 2018	Motion for an extension of time to file the opening briefs on the merits filed. **Main Document**
Aug 20 2018	Brief of petitioner Francis V. Lorenzo filed. **Main Document** **Certificate of Word Count** **Proof of Service**
Aug 20 2018	Joint appendix filed. (Statement of costs filed.) **Main Document** **Proof of Service**
Aug 27 2018	Amicus brief of Securities Law Professors not accepted for filing. (Duplicate submission - September 10, 2018)
Aug 27 2018	Brief amici curiae of Securities Law Professors filed. **Main Document** **Certificate of Word Count** **Proof of Service**
Aug 27 2018	Brief amici curiae of Securities Industry and Financial Markets Association and Chamber of Commerce of the United States of America filed. **Main Document** **Certificate of Word Count** **Proof of Service** **Other** **Other**
Oct 05 2018	Brief of respondent Securities and Exchange Commission filed. **Proof of Service** **Main Document**
Oct 05 2018	Motion to argue pro hac vice filed by respondent Securities and Exchange Commission. **Proof of Service** **Main Document**
Oct 09 2018	SET FOR ARGUMENT on Monday, December 3, 2018
Oct 12 2018	Brief amicus curiae of The North American Securities Administrators

	Association, Inc. filed. **Main Document** **Proof of Service** **Certificate of Word Count**
Oct 15 2018	Record received from the U.S.C.A. District of Columbia Circuit.
Oct 19 2018	CIRCULATED
Oct 19 2018	Justice Kavanaugh is recused in this case.
Oct 26 2018	Motion to argue pro hac vice filed by respondent GRANTED. Justice Kavanaugh took no part in the consideration or decision of this motion.
Nov 01 2018	Reply of petitioner Francis V. Lorenzo filed. (Distributed) **Main Document** **Certificate of Word Count** **Proof of Service**
Dec 03 2018	Argued. For petitioner: Robert Heim, New York, N. Y.; For respondent: Christopher G. Michel, Assistant to the Solicitor General, Department of Justice, Washington, D. C. (pro hac vice.)

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No. _____

In the Supreme Court of the United States

FRANCIS V. LORENZO,
Petitioner,

v.

SECURITIES AND EXCHANGE COMMISSION,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

The antifraud provisions of the federal securities laws prohibit two well-defined categories of misconduct. One category is the use of *fraudulent statements* in connection with the offer and sale of securities. The other category is employing *fraudulent schemes* in connection with the offer and sale of securities. In *Janus Capital Group, Inc. v. First Derivative Traders*, 564 U.S. 135 (2011), this Court considered the elements of a fraudulent statement claim and held that only the "maker" of a fraudulent statement may be held liable for that misstatement under Section 10(b) of the Securities Exchange Act of 1934 and SEC Rule 10b-5(b).

The question presented is whether a misstatement claim that does not meet the elements set forth in *Janus* can be repackaged and pursued as a fraudulent scheme claim. The Circuits have split 3-2 on this question. The Second, Eighth and Ninth Circuits have held that a misstatement alone cannot be the basis of a fraudulent scheme claim, while the DC Circuit and the Eleventh Circuit have held that a misstatement standing alone can be the basis of a fraudulent scheme claim.

PARTIES TO THE PROCEEDING

All parties to the proceeding are named in the caption.

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PETITION FOR A WRIT OF CERTIORARI

Petitioner Francis V. Lorenzo respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the District of Columbia Circuit.

OPINIONS BELOW

The DC Circuit's opinion and Judge Kavanaugh's dissent (Pet. App. 1-50) are reported at 872 F.3d 578 (DC Cir. 2017). The opinion and order of the Securities and Exchange Commission ("SEC") (Pet. App. 51-95) are available at Exchange Act Release No. 74836, 111 S.E.C. Docket 1761 (2015 WL 1927763). The relevant initial decision of the SEC administrative law judge (Pet. App. 96-121) is available at 107 S.E.C. Docket 5934 (SEC Initial Decision Release No. 544, 2013 WL 6858820).

JURISDICTION

The judgment of the Court of Appeals was entered on September 15, 2017. (Pet. App. 1-50). On December 19, 2017, Chief Justice Roberts granted the Petitioner's request to extend the time to file this writ of certiorari to and including January 26, 2018. This Court has jurisdiction under 28 U.S.C. § 1254(1).

STATUTORY AND REGULATORY PROVISIONS INVOLVED

Section 17(a) of the Securities Act of 1933, 15 U.S.C. § 77q(a)

Fraudulent interstate transactions

(a) USE OF INTERSTATE COMMERCE FOR PURPOSE OF FRAUD OR DECEIT It shall be unlawful for any person in the offer or sale of any securities (including security-based swaps) or any security-based swap agreement (as defined in section 78c(a)(78) [1] of this title) by the use of any means or instruments of transportation or communication in interstate commerce or by use of the mails, directly or indirectly—

(1) to employ any device, scheme, or artifice to defraud, or

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j

Manipulative and deceptive devices
It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality

of interstate commerce or of the mails, or of any facility of any national securities exchange—

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, or any securities-based swap agreement any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

SEC Rule 10b-5, 17 CFR 240.10b-5

Employment of manipulative and deceptive devices.
It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.

STATEMENT

1. The antifraud provisions of the federal securities laws prohibit two well-defined categories of misconduct in connection with the offer and sale of securities. One category is the use of *fraudulent statements* in connection with the offer and sale of securities; the other category is employing *fraudulent schemes*. With regard to fraudulent statements, Section 17(a)(2) of the Securities Act of 1933 (the "Securities Act") establishes liability for misstatements and proscribes obtaining money or property by means of any untrue statement or omission of a material fact. Likewise, Section 10(b) of the Securities and Exchange Act of 1934 (the "Exchange Act") and SEC Rule 10b-5(b) thereunder prohibit making any "untrue statement of a material fact. . ."

With regard to *fraudulent schemes*, Section 17(a)(1) of the Securities Act prohibits anyone from employing any "device, scheme, or artifice to defraud" in the offer or sale of securities. Likewise, Section 10(b) of the Exchange Act and SEC Rule 10b-5(a) prohibit anyone from employing "any device, scheme, or artifice to defraud" in connection with the purchase or sale of securities and Rule 10b-5(c) prohibits anyone from engaging in "any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person. . ." in connection with the purchase or sale of securities. Claims brought under Rules 10b-5(a) and (c) are generally referred to as "scheme liability" claims. *See, e.g., In re DVI, Inc. Sec. Litig.*, 639 F.3d 623, 643 n.29 (3d Cir. 2011), *abrogated on other grounds by Amgen Inc. v. Connecticut Retirement Plans and Trust Funds*, 568 U.S. 455 (2013)("We refer to

claims under Rule 10b-5(a) and (c) as 'scheme liability claims', because they make deceptive conduct actionable, as opposed to Rule 10b-5(b), which relates to deceptive statements.")

The DC Circuit's opinion in this matter "creates a circuit split[1] by holding that mere misstatements, standing alone, may constitute the basis for so-called scheme liability under the securities laws – that is, willful participation in a scheme to defraud – even if the defendant did not make the misstatements." (Kavanaugh, J., dissenting) (Pet. App. 46). However, claims for fraudulent statements are distinct from claims for fraudulent schemes. *Desai v. Deutsche Bank Sec., Ltd.*, 573 F.3d 931, 939 (9th Cir. 2009). In fact, this Court in *Janus Capital Group, Inc. v. First Derivative Traders*, 564 U.S. 135 (2011) carefully set forth the elements that a plaintiff must establish to prove a fraudulent statement claim under the federal securities laws. The DC Circuit's decision below allows the SEC and private plaintiffs to sidestep *Janus*' carefully drawn out elements of a fraudulent statement claim merely by relabeling the claim -- with nothing more -- as a fraudulent scheme claim.

The DC Circuit's decision also erases the important distinction between primary and secondary violators of the securities laws and opens up large numbers of defendants who are secondary actors at best to claims for securities fraud – claims that would otherwise be barred in private litigation under the holding of *Central*

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[1] Judge Kavanaugh's dissenting opinion did not discuss the two Eleventh Circuit cases referenced *infra* at 20 that are in agreement with the DC Circuit, which results in a 3-2 circuit split.

Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A., 511 U.S. 164, 191 (1994), which eliminated aiding and abetting liability in private securities fraud litigation.

The DC Circuit's decision raises legal questions of national importance both for the SEC's enforcement program and for private securities litigation, including federal securities class actions. The question presented in this petition is critical to the fair and uniform enforcement of the federal securities laws and this case squarely presents the issue that has divided the circuits.

This case merits the Court's review and the Court should resolve the circuit split.

2. In February 2009, Francis V. Lorenzo ("Lorenzo") became the director of investment banking at Charles Vista, LLC ("Charles Vista"). (Pet. App. 3). Charles Vista was a broker-dealer registered with the SEC and owned by Gregg Lorenzo, who is no relation to Francis Lorenzo. (*Ibid.*) One of Charles Vista's clients was Waste2Energy Holdings, Inc. ("W2E"). W2E represented to Charles Vista and to the public that it had developed a valuable "gasification" technology that could generate electricity by converting solid waste into gas. (*Ibid.*) W2E was a public company with various SEC filings publicly available that described its operations and financial condition in detail. (Pet. App 4).

In September 2009, W2E conducted a private offering of $15 million in convertible debentures to select investors. (Pet. App. 3). Debentures are "debt secured only by the debtor's earning power, not by a

lien on any specific asset." BLACK'S LAW DICTIONARY 486 (10th ed. 2014). Charles Vista served as the exclusive placement agent for W2E's debenture offering. (Pet. App. 3-4).

In its most recent SEC filing at the time, the June 3, 2009 Form 8-K (which is used to notify investors of certain specified material events), W2E stated that its intangible assets, including its gasification technology, were worth just over $10 million as of the end of 2008. (Pet. App. 4). On September 9, 2009, W2E prepared a private offering memorandum for potential investors that described the offering, the debentures and W2E's financial condition. (*Ibid.*)

W2E's gasification technology never materialized and on October 1, 2009, after a lengthy audit, W2E filed an amended Form 8-K, in which it reported a total "impairment" of its intangible assets, because management made a determination that the company's assets were of no value. (Pet. App. 3-4). W2E reduced the value of its gasification technology to zero and its total assets to $370,552 as of March 31, 2009. (Pet. App. 4). On the same day that it filed its amended Form 8-K, October 1, 2009, W2E also filed a quarterly Form 10-Q with the SEC, in which it valued its total assets at $660,408 as of June 30, 2009. (*Ibid.*)

Later on October 1, 2009, Lorenzo's secretary alerted him by email that W2E had filed an amended Form 8-K. (Pet. App. 4). The next day, Lorenzo emailed links to both of W2E's October 1 filings to all Charles Vista brokers. (*Ibid.*) There is no evidence that Lorenzo read the two SEC filings in detail or that he was aware that W2E had written down the value of its assets.

On October 14, 2009, Lorenzo separately emailed two potential investors "several key points" about W2E's pending debenture offering. (Pet. App. 5). His emails omitted any mention of the devaluation of W2E's intangible assets. Lorenzo's emails stated to both recipients that the offering came with "3 layers of protection: (I) [W2E] has over $10 mm in confirmed assets; (II) [W2E] has purchase orders and LOI's for over $43 mm in orders; (III) Charles Vista has agreed to raise additional monies to repay these Debenture holders (if necessary)." (*Ibid.*) One of Lorenzo's messages said that it had been sent "[a]t the request of Gregg Lorenzo," and the other stated that it had been sent "[a]t the request of Adam Spero [a broker with Charles Vista] and Gregg Lorenzo." In both messages, Lorenzo stated that the recipients could call him with any questions. He signed both messages with his name and title as "Vice President – Investment Banking." (*Ibid.*)

3. On February 15, 2013, the SEC commenced enforcement proceedings against Lorenzo, Gregg Lorenzo, and Charles Vista. (Pet. App. 5). It charged each with violating three securities-fraud provisions: (i) Section 17(a)(1) of the Securities Act of 1933, 15 U.S.C. § 77q(a)(1); (ii) Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j; and (iii) Securities Exchange Act Rule 10b-5, 17 C.F.R. § 240.10b-5. Gregg Lorenzo and Charles Vista settled the charges against them, but the claims against Lorenzo concerning the two emails proceeded to an administrative hearing before the SEC. (Pet. App. 5-6).

On September 18 and 19, 2013, an administrative hearing was held before an SEC administrative law

judge, and, on December 31, 2013, an Initial Decision was rendered (Pet. App. 98-121). After hearing Lorenzo's testimony and weighing his credibility, the judge concluded that Lorenzo's boss (Gregg Lorenzo) had "drafted" the emails in question (Pet. App. 106) and that Lorenzo's boss had "asked" Lorenzo to send the emails to the two clients. (Pet. App. 38; 106). The administrative law judge also concluded that Lorenzo did not read the text of the emails and that Lorenzo "sent the emails without even thinking about the contents." (Pet. App. 38; 109). Furthermore, the judge noted that the emails themselves expressly stated that they were being sent at "the request" of Lorenzo's boss. (Pet. App. 39; 107). "Those factual findings were very favorable to Lorenzo and should have cleared Lorenzo of any serious wrongdoing under the securities laws." (Kavanaugh, J., dissenting) (Pet. App. 39).

"Nevertheless, [t]he judge somehow concluded that those findings of fact demonstrated that Lorenzo willfully violated the securities laws – meaning that Lorenzo acted with an intent to deceive, manipulate, or defraud." (Kavanaugh, J dissenting) (Pet. App. 39). As a sanction, the judge: (i) ordered Lorenzo to cease and desist from violating each securities-fraud provision giving rise to the charges against him; (ii) imposed against Lorenzo a lifetime bar from the securities industry; and (iii) imposed a civil monetary penalty of $15,000. (Pet. App 39; 119; 120).

However,

> the administrative law judge's factual findings and legal conclusions do not square up. If Lorenzo did not draft the emails, did not think about the contents of the emails, and sent the

> emails only at the behest of his boss, it is impossible to find that Lorenzo acted 'willfully'. That is Mens Rea 101. Establishing that a defendant acted willfully in this context requires proof at least of the defendant's 'intent to deceive, manipulate, or defraud.' *Dolphin & Bradbury, Inc. v. SEC*, 512 F.3d 634, 639 (D.C. Cir. 2008) (internal quotation marks omitted). (Kavanaugh, J., dissenting) (Pet. App. 39).

4. Lorenzo petitioned the Commission for review of the Initial Decision and argued that the administrative law judge's factual findings did not support the judge's legal conclusions and sanctions. The Commission came to the same conclusion. "But instead of vacating the order against Lorenzo, the Commission did something quite different and quite remarkable. In a Houdini-like move, the Commission rewrote the administrative law judge's factual findings to make those factual findings correspond to the legal conclusion that Lorenzo was guilty and deserving of a lifetime suspension." (Kavanaugh, J., dissenting) (Pet. App. 41).

> Without hearing from Lorenzo or any other witnesses, the Commission simply swept the judge's factual and credibility findings under the rug. The Commission concluded that Lorenzo himself was 'responsible' for the emails' contents. . . Faced with inconvenient factual findings that would make it hard to uphold the sanctions against Lorenzo, the Commission – without hearing any testimony – simply manufactured a new assessment of Lorenzo's credibility and rewrote the judge's factual

findings. (Kavanaugh, J., dissenting) (Pet. App. 41-42).

On April 29, 2015, the Commission issued an Opinion sustaining the Initial Decision's conclusion that the two emails in question violated Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5(a), (b) and (c) thereunder. The Commission Opinion also imposed on Lorenzo a cease-and-desist order, a lifetime bar from the securities industry and a civil monetary penalty of $15,000. (Pet. App. 51-97). The Commission denied Lorenzo's motion for reconsideration on June 3, 2015. (Pet. App. 6). The appeal to the DC Circuit followed.

5. On September 15, 2017, the DC Circuit overturned the Commission's finding that Lorenzo violated Rule 10b-5(b) on the grounds that Lorenzo did not make the misstatements at issue and vacated the Commission's sanctions. (Pet. App. 1-37). However, the DC Circuit in a 2-1 decision upheld the Commission's findings that Lorenzo violated Section 17(a)(1) of the Securities Act, Section 10(b) of the Securities Exchange Act, and Rule 10b-5(a) and (c). (Pet. App. 25). Judge Kavanaugh issued a dissenting opinion that sharply disagreed with the majority's holding that Lorenzo violated any of those securities fraud provisions. In particular, Judge Kavanaugh criticized the majority's deference to the Commission's finding that Lorenzo acted with scienter. "How could Lorenzo have intentionally deceived the clients when he did not draft the emails, did not think about the contents of the emails, and sent the emails only at his boss's direction?" (Kavanaugh, J., dissenting) (Pet. App. 39-40)

Judge Kavanaugh was also highly critical of the majority's deference to the Commission's rewriting of the administrative law judge's factual findings. Judge Kavanaugh stated

> Lorenzo was the only relevant witness at trial . . . and given that his credibility was central to the case, the SEC had no reasonable basis to run roughshod over the administrative law judge's findings of fact and credibility assessments. In short, the SEC's rewriting of the findings of fact deserves judicial repudiation, not judicial deference or respect. (Kavanaugh, J., dissenting)(Pet. App. 45)

In fact, Judge Kavanaugh severely criticized the Commission's entire administrative process in the way it handled the enforcement proceedings against Lorenzo. "The administrative law judge's decision in this case contravenes basic due process (Pet. App. 40). . . Lorenzo is entitled to a fair process just like everyone else. He has not received a fair process in this case. (Kavanaugh, J., dissenting)(Pet. App. 40, 49)(citations omitted).

The DC Circuit remanded the case to the Commission for reconsideration of the appropriate penalties to impose on Lorenzo. (Pet. App. 36-37). This Petition for a Writ of Certiorari followed.

REASONS TO GRANT THE PETITION

A. There is a Split Among the Courts of Appeals On Whether Inadequate Claims for Misstatements Can be Repackaged as Claims for Fraudulent Schemes

> The DC Circuit's opinion below creates a circuit split by holding that mere misstatements, standing alone, may constitute the basis for so-called scheme liability under the securities laws – that is, willful participation in a scheme to defraud – even if the defendant did not make the misstatements. No other Court of Appeals has adopted the approach that the majority opinion adopts here. Other courts have instead concluded that scheme liability must be based on conduct that goes beyond a defendant's role in preparing mere misstatements or omissions made by others. (Kavanaugh, J., dissenting) (Pet. App. 46).

The federal securities laws contain a well-established distinction between claims for fraudulent *statements* and claims for fraudulent *conduct*. Rule 10b-5(b), promulgated under Section 10(b) of the Securities Exchange Act of 1934, proscribes making untrue *statements* in connection with the purchase or sale of a security. In contrast, Section 17(a)(1) of the Securities Act and Rule 10b-5(a) and (c) proscribe deceptive *conduct* (such as market manipulation) in connection with the offer, purchase or sale of a security.

While there is some overlap in these antifraud provisions, this Court has set bright line legal standards for claims for false statements under Rule

10b-5(b). Specifically, only a person who "makes" a misstatement can be held liable for that misstatement under Rule 10b-5(b). *Janus Capital Group, Inc. v. First Derivative Traders*, 564 U.S. 135, 142 (2011). Under *Janus*, for purposes of Rule 10b-5

> the maker of a statement is the person or entity with ultimate authority over the statement, including its content and whether and how to communicate it. Without control, a person or entity can merely suggest what to say, not "make" a statement in its own right. One who prepares or publishes a statement on behalf of another is not its maker. *Janus*, 564 U.S. at 142.

The DC Circuit correctly held that Lorenzo was not liable under Rule 10b-5(b) for the three misstatements in the two emails, because Lorenzo was not the "maker" of the statements under the standards set by this Court's holding in *Janus*. However, the DC Circuit erroneously held that these same misstatements, which it found Lorenzo did not make, could still be the sole basis of fraudulent scheme liability under Section 17(a)(1) of the Securities Act, Section 10(b) of the Exchange Act and Rule10b-5(a) and (c).

By so holding, the DC Circuit erroneously adopted the minority side of a now 3-2 circuit split and has eviscerated this Court's holding in *Janus*. The DC Circuit's decision allows both the SEC and private plaintiffs to sidestep the carefully laid out standards for fraudulent statement claims by repackaging the claims -- with nothing more -- as claims for fraudulent schemes.

1. The *Janus* Decision Sets Forth a Clear Bright Line Test for Misstatement Liability Under the Federal Securities Laws.

False statements are exclusively addressed in Section 17(a)(2) of the Securities Act and in SEC Rule 10b-5(b). These provisions prohibit making false statements of material fact in connection with the offer, purchase or sale of a security. In contrast, Section 17(a)(1) and the other two subsections of Rule 10b-5 – (a) and (c) – do not address false statements at all and prohibit distinctly different types of fraud in the category of deceptive schemes, such as market manipulation. This Court has stated that the term "manipulative" is "a term of art when used in connection with securities markets," referring to practices "such as wash sales, matched orders, or rigged prices, that are intended to mislead investors by artificially affecting market activity." *Santa Fe Industries, Inc. v. Green*, 430 U.S. 462, 476 (1977). *See also SEC v. Pentagon Capital Management PLC*, 725 F.3d 279 (2d Cir. 2013)(Pentagon's late trading activity, beyond the communication of the trades themselves, included finding brokers and a clearing system that would allow late trades, as well as the specific coordination—on a daily basis—of the transmission of instructions to buy or sell or refrain from doing. . .In short, Pentagon's fraudulent activities independently satisfy the requirements of scheme liability under Rule 10b–5(a) and (c) and Section 17(a)).

The Court in *Janus* established a bright-line test to determine whether a person can be held liable for false statements under Section 10(b) of the Exchange Act and Rule 10b-5(b) thereunder. In *Janus*, this Court

held that a defendant may be liable for false statements under Rule 10b-5(b) only if the defendant was the "maker" of the false statements. *Janus*, 564 U.S. at 142. Specifically, a defendant may be held liable for a false statement only if he is the person or entity with ultimate authority on whether and how to communicate the statement, including its content, and whether and how to communicate it. *Ibid.* The *Janus* decision held that only the "maker" of the statement, but not a person who substantially participates in the creation of the statement, can be held primarily liable under Section 10(b) and Rule 10b-5.

The *Janus* decision reasoned that, without control, a person or entity can merely suggest what to say, not "make" a statement in its own right. The *Janus* decision held that one who prepares or publishes a statement on behalf of another is not its maker and that, in the ordinary case, attribution within a statement or implicit from surrounding circumstances is strong evidence that a statement was made by—and only by—the party to whom it is attributed. *Janus*, 564 U.S. at 142-43. District courts have extended the *Janus* Court's holding to misstatement claims brought not only under Rule 10b-5(b) but also to misstatement claims brought under Section 17(a) of the Securities Act. *See SEC v. Kelly*, 817 F. Supp. 2d 340, 344 (S.D.N.Y. 2011); *SEC v. Perry*, 2012 WL 1959566, at *8 (C.D. Cal. May 31, 2012).

In this case, the DC Circuit held that, under the standards set forth in *Janus*, Lorenzo was not the maker of the misstatements at issue and therefore was not liable under Rule 10b-5(b). However, the DC Circuit erroneously held that Lorenzo could be liable

for those same misstatements under a theory of scheme liability under Section 17(a)(1) of the Securities Act and Rule 10b-5(a) and (c).

The DC Circuit's holding in this matter is contrary to the view of a majority of circuits that have considered the issue. The majority view is that plaintiffs, including the SEC, cannot repackage Rule 10b-5(b) deceptive statement claims that fail to meet the *Janus* standards as fraudulent scheme claims under Section 17(a)(1) of the Securities Act or Rule 10b-5(a) and (c).

2. The Majority View is that Inadequate False Statement Claims Cannot be Repackaged as Fraudulent Scheme Claims

The Second Circuit was the first circuit to address whether misstatements by themselves could form the basis for claims for fraudulent scheme claims under Section 10(b) of the Exchange Act and Rule 10b-5(a) and (c). In *Lentell v. Merrill Lynch & Co.*, 396 F.3d 161, 177 (2d Cir. 2005), the Second Circuit held that misstatements alone could not form the basis of fraudulent scheme claims. In *Lentell*, the Second Circuit held that the plaintiffs failed to make out fraudulent scheme claims for market manipulation under Rule 10b-5(a) and (c) when the sole basis for the market manipulation claims were alleged misrepresentations or omissions made by the defendants. *See also SEC v. Kelly*, 817 F. Supp. 2d 340, 343-44 (S.D.N.Y. 2011)(dismissing the SEC's fraudulent scheme claims, because they were premised on a misrepresentation and neither defendant "made" the misstatement as *Janus* requires).

The Ninth Circuit in *Desai v. Deutsche Bank Sec., Ltd.*, 573 F.3d 931, 939 (9th Cir. 2009), has also held that mere misstatements standing alone cannot be the basis of claims for fraudulent schemes.

> We must recognize, however, that manipulative conduct has always been distinct from actionable omissions. Omissions are generally actionable under Rule 10b-5(b)... Manipulative conduct, by contrast, is actionable under Rule 10b-5(a) or (c) and includes activities designed to affect the price of a security artificially by simulating market activity that does not reflect genuine investor demand....If such nondisclosure of a defendant's fraud was an actionable omission, then every manipulative conduct case would become an omissions case. If that were so, then all of the Supreme Court's discussion of what constitutes manipulative activity would be redundant. We decline to read the Supreme Court's case law on manipulative conduct as a little more than an entertaining, but completely superfluous, intellectual exercise. *See Stoneridge*, 128 S.Ct. at 769 (listing the three types of §10(b) actions); *Cent. Bank*, 511 U.S. at 177, 114 S.Ct. 1439 (same)(citations omitted). (*Desai*, 573 F.3d at 939).

The Ninth Circuit has held that, for fraudulent scheme claims to be actionable under Rule 10b-5(a) or (c), something more is required than just deceptive statements. *WPP Luxembourg Gamma Three Sarl v. Spot Runner, Inc.*, 655 F.3d 1039 (9th Cir. 2011). In *WPP* the Ninth Circuit stated that a "defendant may only be liable as part of a fraudulent scheme based

upon misrepresentations and omissions under Rules 10b–5(a) or (c) when *the scheme also encompasses conduct beyond those misrepresentations or omissions.*" (655 F3d at 1057)(emphasis added). In the *WPP* case, the Ninth Circuit also stated that a "theory of recovery that merely repeats the allegations made in support of ... misrepresentation and omission claim" is not a valid claim under Rule 10b–5(a) or (c) 655 F.3d at 1057-58 (*citing In re Nat'l Century Fin. Enters., Inc. Inv. Litig.*, 2006 WL 469468, at *21 (S.D.Ohio Feb. 27, 2006)).

In the *WPP* case, the Ninth Circuit stated that a defendant who uses a "device, scheme, or artifice to defraud" or who engages in "any act, practice, or course of business which operates or would operate as a fraud or deceit" may be liable for securities fraud under Rule 10b-5(a) or (c). By contrast, "[o]missions are generally actionable under Rule 10b–5(b) ... [and] stem from the failure to disclose accurate information relating to the value of a security where one has a duty to disclose it." *WPP*, 655 F.3d at 1057 (*citing Desai*, 573 F.3d at 940). The Ninth Circuit further stated in *WPP* that "[c]ourts have generally held that a Rule 10b–5(a) and/or (c) claim cannot be premised on the alleged misrepresentations or omissions that form the basis of a Rule 10b–5(b) claim." (*WPP*, 655 F.3d at 1057).

The Eighth Circuit is in agreement with the Ninth and Second Circuits in holding that misstatements, standing alone, can never be sufficient to bring a fraudulent scheme claim under Rule 10b-5(a) or (c). In *Public Pension Fund Group v. KV Pharmaceutical Co.*, 679 F.3d 972 (8th Cir. 2012), the Eighth Circuit stated that "[w]e join the Second and Ninth Circuits in recognizing a scheme liability claim must be based on

conduct beyond misrepresentations or omissions actionable under Rule 10b-5(b)." (679 F.3d at 987). In doing so, the Eighth Circuit recognized the important distinction between claims for misstatements and claims for deceptive schemes. "Claims brought under Rules 10b-5(a) and (c) are generally referred to as 'scheme liability' claims." 679 F.3d at 986 (citing *DVI, Inc.*, 639 F.3d 623, 643 n. 29).

3. The Minority View is that False Statements Standing Alone Can Be the Basis for Fraudulent Scheme Claims.

In contrast to this majority rule, the Eleventh Circuit in *SEC v. Big Apple Consulting USA, Inc.*, 783 F.3d 786 (11th Cir. 2015) held that "even a person ... who is not the 'maker' of an untrue statement of material fact, nonetheless could be liable as a primary violator of Rule 10b–5(a) and (c)." (783 F.3d 795-96). The Eleventh Circuit also said in the *Big Apple Consulting* case that "[S]ubsection (b) was the only subsection at issue in *Janus*" (783 F.3d at 796) and that "*Janus* does not extend to claims based on schemes to defraud under Rule 10b–5(a) and (c)." *Ibid.*

In another case, the Eleventh Circuit held that "*Janus* only discussed what it means to 'make' a statement for purposes of Rule 10b–5(b) and did not concern section 17(a)(1) or (3) or Rule 10b–5(a) or (c)." *SEC v. Monterosso*, 756 F.3d 1326, 1334 (11th Cir. 2014). The Eleventh Circuit further stated in *Monterosso* that "the operative language of section 17(a) does not require a defendant to "make" a statement in order to be liable." (756 F.3d at 1334).

In this case, the DC Circuit joined the Eleventh Circuit's position and created a 3-2 circuit split. The DC Circuit stated that "[w]e know of no blanket reason, however, to treat the various provisions as occupying mutually exclusive territory, such that false-statement cases must reside exclusively within the province of Rule 10b-5(b)." (Pet. App. 25-26).

Respectfully, the minority position is erroneous, and this Court should adopt the view of the majority of the circuits and hold that plaintiffs, including the SEC, cannot sidestep the *Janus* requirements for false statement claims simply by repackaging the claims as fraudulent scheme claims.

B. This Case Presents an Ideal Vehicle For Resolving A Recurring Legal Issue of Unquestionable Importance to the Fair and Uniform Enforcement of the Federal Securities Laws.

The question presented in this petition is critical to the fair and uniform enforcement of the federal securities laws. Moreover, this case is an ideal vehicle to resolve the circuit split. The DC Circuit expressly considered and rejected the holdings of the Second, Eighth and Ninth Circuits. Also, the legal question presented here is unquestionably important. The issue arises frequently in SEC enforcement proceedings and in private securities litigation, including securities class action lawsuits. Private litigation and SEC enforcement actions often involve very significant liability and, in addition, SEC enforcement actions (like the one filed against Lorenzo) often seek to bar individuals from working in their chose profession in the securities industry.

If the Courts of Appeals diverge on whether a defendant who did not make a misstatement can be sued for securities fraud, securities plaintiffs, including the SEC, will migrate to those courts that enable them to ensnare the greatest number of defendants. This is a real risk, because, if Lorenzo had been sued by the SEC in a district court in the State of New York, where he lives, instead of in an SEC administrative proceeding, the SEC's case would have been dismissed under the Second Circuit precedent discussed above. However, because Lorenzo's appeal from the Commission's Order was of necessity to the DC Circuit, he has been found liable of violating Section 10(b) of the Exchange Act and Rule 10b-5(a) and (c) and Section 17(a)(1) of the Securities Act. The SEC routinely has a choice of venue and to prevent the Eleventh and DC Circuits from becoming the forums of choice for the SEC and overbroad private securities lawsuits, this Court should grant review and resolve the 3-2 circuit split.

In addition, the question presented in this Petition will reoccur and likely lead to a deepening of the circuit split. Federal district courts in circuits that have not ruled on the issues raised in this Petition have likewise taken conflicting positions. *Compare Lautenberg Found. v. Madoff*, 2009 WL 2928913, at *12 (D.N.J. Sept. 9, 2009)("[c]ourts have generally held that '[a] Rule 10b–5(a) and/or (c) claim cannot be premised on the alleged misrepresentations or omissions that form the basis of a Rule 10b–5(b) claim'") *with SEC v. Benger*, 931 F. Supp. 2d 904, 905-06 (N.D. Ill. 2013)(misstatements can give rise to liability under the antifraud provisions even if the conduct in question does not amount to "making" a statement under

Janus). *See also SEC v. Familant*, 910 F. Supp. 2d 83, 93-95 (D.D.C. 2012)(holding that misstatements can give rise to liability under the antifraud provisions even if the conduct in question does not amount to "making" a statement under *Janus*).

In addition, the SEC has moved aggressively in its enforcement cases to implement the minority view espoused by the Eleventh Circuit, which allows plaintiffs to pursue misstatement claims as fraudulent scheme claims and thereby sidestep the standards for misstatement claims set forth in this Court's *Janus* decision. *See Opinion of the Commission in In the Matter of John P. Flannery and James D. Hopkins* (Exchange Act Release No. 73840, 2014 WL 7145625 (Dec. 15, 2014), *vacated on other grounds*, *Flannery v. SEC*, 810 F.3d 1 (1st Cir. 2012).

There is also no need for additional percolation. Five circuits, as well as numerous district courts, have considered whether fraudulent statements on their own can form the basis of a fraudulent scheme claim and the arguments on both sides of the split have been fully aired.

C. The DC Circuit's Decision is Wrong

In its opinion below, the DC Circuit ignored the well-established distinction in the federal securities laws between claims for fraudulent statements and claims for fraudulent schemes. The DC Circuit held that Lorenzo was liable for misstatements that he did not make under the provisions of the federal securities laws that proscribe fraudulent schemes. The DC Circuit also erroneously held the Court's holding in *Janus* applied only to Rule 10b-5(b) and not to the

other subsections of Rule 10b-5 or to Section 17(a)(1) of the Securities Act.

1. Mere Misstatements Standing Alone Cannot Be The Basis of Fraudulent Scheme Claims Under the Federal Securities Laws.

As the Ninth Circuit recognized in *Desai*, claims for misstatements have always been distinct from fraudulent scheme claims. *Desai*, 573 F.3d at 940 ("We must recognize, however, that manipulative conduct has always been distinct from actionable omissions"). Section 17(a)(2) of the Securities Act concerns misstatements, while Sections 17(a)(1) and (3) of the Securities Act concern fraudulent schemes. This distinction is also recognized in the structure of Rule 10b-5 itself with its three subsections, two of which concern fraudulent schemes (10b-5 (a) and (c)) and one of which concerns misstatements (10b-5(b)).

The DC Circuit's decision below affirming securities fraud liability against Lorenzo for statements he did not make sweeps away any meaningful distinction between claims for false statements and claims for fraudulent schemes. The DC Circuit's decision also renders meaningless the carefully laid out subsections of Section 17(a) of the Securities Act and Rule 10(b)-5. Under the DC Circuit's approach, all claims for false statements can be brought as fraudulent scheme claims, and, vice-versa, claims for nondisclosure of a defendant's fraudulent conduct become viable claims for misstatements and omissions. (*Desai*, 573 F.3d at 940).

2. The DC Circuit's Decision Erases the Distinction between Primary and Secondary Liability Under the Federal Securities Laws and Greatly Expands the Number of Defendants Who Qualify as Primary Violators.

In *Janus*, this Court narrowed the scope of actors who can qualify as primary defendants in claims for misstatements by holding that only those who "made" a misstatement can be liable for the misstatement. This limitation on the scope of misstatement liability is also important because it directly ties into another important limitation on the scope of liability under the securities laws, which is the inability of private plaintiffs to bring claims against secondary actors for aiding and abetting liability. *Central Bank*, 511 U.S. 164, 191 (1994). In this regard, the *Janus* Court stated:

> For purposes of Rule 10b–5, the maker of a statement is the person or entity with ultimate authority over the statement, including its content and whether and how to communicate it. Without control, a person or entity can merely suggest what to say, not "make" a statement in its own right. . . This rule follows from *Central Bank*, in which we held that Rule 10b–5's private right of action does not include suits against aiders and abettors . . . A broader reading of "make," including persons or entities without ultimate control over the content of a statement, would substantially undermine *Central Bank*. If persons or entities without control over the content of a statement could be considered primary violators who "made" the

> statement, then aiders and abettors would be almost nonexistent. *Janus*, 564 U.S. at 142-43 (internal citations omitted)

The distinction between primary and secondary liability matters, particularly for private securities lawsuits, in which private plaintiffs may not maintain aiding and abetting lawsuits. *Central Bank*, 511 U.S. at 191. Instead of maintaining the important limitations on secondary liability, the DC Circuit has created a backdoor by which private plaintiffs can bring claims of primary violations of the securities laws under a scheme liability theory against large numbers of defendants who would otherwise be secondary actors and immune from suit by private plaintiffs because they did not make the misstatements at issue.

The DC Circuit's decision below allows plaintiffs to sidestep the important limitations *Janus* placed on primary misstatement claims by allowing plaintiffs to pursue inadequate claims against defendants by simply relabeling the misstatement claims as fraudulent scheme claims. To allow a private plaintiff to use a fraudulent scheme theory to pursue primary liability against a defendant who did not make a misstatement would erase the distinction between primary and secondary liability. This, in turn, would allow private plaintiffs to bring claims against defendants that would otherwise be barred as aiding and abetting claims. *See Global Crossing Ltd. Sec. Litig.*, 322 F. Supp. 2d 319, 337 n.17 (S.D.N.Y. 2004) (Subsections (a) and (c) may only be used to state a claim . . . for the underlying deceptive devices or frauds themselves, and not as a short cut to circumvent *Central Bank's* limitations on liability for a secondary actor's involvement in making

misleading statements. (*quoting In re Lernout & Hauspie Sec. Litig.*, 230 F. Supp. 2d 152, 175 (D. Mass. 2002))).

The SEC has also aggressively tried to expand the scope of primary liability under the securities laws even though it is empowered by Section 20(e) of the Exchange Act to bring civil actions against aiders and abettors of securities fraud. 15 U.S.C. § 78t(e). Allowing the SEC to repackage inadequate claims for misstatements as fraudulent scheme claims allows the SEC to be able to evade the important statutory distinction between primary liability and secondary (aiding and abetting) liability under Section 20(e) of the Exchange Act. The SEC can do this by charging aiders and abettors with primary liability under a theory of scheme liability.

> For decades, . . .the SEC has tried to erase that distinction [between primary and secondary liability] so as to expand the scope of primary liability under the securities laws. For decades, the Supreme Court has pushed back hard against the SEC's attempts to unilaterally rewrite the law. *See Janus*, 564 U.S. 135; *Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc.* 552 U.S. 148 (2008); *Central Bank of Denver, NIA. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164 (1994). Still undeterred in the wake of that body of Supreme Court precedent, the SEC has continued to push the envelope and has tried to circumvent those Supreme Court decisions. *See, e.g., In the Matter of John P. Flannery & James D. Hopkins*, Release No. 3981 (Dec. 15, 2014). This case is

merely the latest example. (Kavanaugh, J., dissenting) (Pet. App. 47).

In this case the SEC could have brought an action under Section 20(e) of the Exchange Act against Lorenzo for aiding and abetting violations of the antifraud provisions by Gregg Lorenzo, who was Francis Lorenzo's boss and the maker of the misstatements in the two emails that were sent. While Lorenzo would have factual defenses to an SEC action for aiding and abetting, such a claim would not have raised any of the problematic legal questions that are the subject of this petition.

Nevertheless, the SEC chose not to bring aiding and abetting claims against Lorenzo and instead improperly pursued primary liability claims under a theory of scheme liability. By doing so the SEC chose to evade the important limitations that this Court has placed on securities fraud liability in *Janus* and *Central Bank*. This Court should not permit the SEC to evade the carefully laid out elements of misstatement claims and statutory aiding and abetting claims.

3. The DC Circuit's Holding Eviscerates this Court's Bright Line Holding in *Janus* by Permitting Plaintiffs To Repackage Misstatement Claims That Do Not Meet the *Janus* Requirements as Fraudulent Scheme Claims.

The DC Circuit's opinion allows the SEC to sidestep the standards that this Court set for misstatement claims in *Janus*. Under the DC Circuit's decision below the SEC may bring inadequate fraudulent

statement claims merely by relabeling them as fraudulent scheme claims. This result renders *Janus* meaningless. (*See Kelly*, 817 F.Supp.2d at 344)("Where the primary purpose and effect of a purported scheme is to make a public misrepresentation or omission, courts have routinely rejected the SEC's attempt to bypass the elements necessary to impose 'misstatement' liability under subsection (b) by labeling the alleged misconduct a 'scheme' rather than a 'misstatement.'") Moreover, if a plaintiff were permitted to pursue a claim for scheme liability against a defendant who did not have the ultimate authority over the content and dissemination of an allegedly false statement, then the *Janus* holding would be rendered meaningless, which is a result that this Court would not support.

As discussed above, the Second, Ninth and Eighth Circuits have all held that to have a viable fraudulent scheme claim a plaintiff must prove that the defendant committed an inherently deceptive or manipulative act that is independent from any alleged misstatement. This prevents plaintiffs from having a backdoor into liability against defendants who did not make the misstatements at issue. *See Lentell v. Merrill Lynch & Co.*, 396 F. 3d 161, 177 (2d Cir. 2005) (rejecting scheme liability where the sole basis for such claims is alleged misrepresentations or omissions); *see also PIMCO*, 341 F. Supp. 2d at 468-69 (rejecting scheme liability for market timing, because the fraud arose only from misleading disclosures). "Subsections (a) and (c) are not a backdoor into liability for those who help others make a false statement or omission in violation of subsection (b) of Rule 10b-5." *In re Parmalat Sec. Litig.*, 376 F. Supp. 2d 472, 503 (S.D.N.Y 2005). "Because the

core misconduct alleged is in fact a misstatement, it would be improper to impose primary liability . . . by designating the alleged fraud a manipulative device rather than a misstatement." *SEC v. KPMG LLP*, 412 F.Supp.2d 349, 378 (S.D.N.Y. 2006); *SEC v. Benger*, No. 09 C 676, 2013 WL 1150587, at *5 (N.D. Ill. Mar. 21, 2013)(*Janus* cannot be skirted simply by artful pleading and rechristening a 10b-5(b) claim as a claim under 10b-5(a) and (c)).

4. The DC Circuit Erroneously Held that Lorenzo's Ministerial Acts in Forwarding An Email to Two People Provided a Basis for Fraudulent Scheme Liability.

The DC Circuit erroneously held that Lorenzo's conduct in transmitting the two emails in question was an independent ground for finding that he violated the securities laws' prohibitions against fraudulent schemes regardless of whether he made the statements in question. The DC Circuit's holding in this regard is erroneous, because Lorenzo's actions in sending emails to two investors were only ministerial, and allowing such conduct to serve as the basis of a fraudulent scheme claim under Section 17(a)(1), Section 10(b) and Rules 10b-5(a) and (c) would again erase any meaningful distinction between proscriptions against misstatements and fraudulent schemes. The DC Circuit's opinion cites no conduct by Lorenzo that is not ministerial in nature.

The reasoning of the DC Circuit in holding that Lorenzo engaged in a fraudulent scheme independent of whether he made the statements in question is unpersuasive. While the Court in *Janus* did not address "scheme liability" under subsections (a) and (c)

of Rule 10b–5, nonetheless, where the primary purpose and effect of a purported scheme is to make a public misrepresentation or omission, courts have routinely rejected the SEC's attempt to bypass the elements necessary to impose "misstatement" liability under subsection (b) by labeling the alleged misconduct a "scheme" rather than a "misstatement." *See, e.g., Lentell v. Merrill Lynch & Co.*, 396 F.3d 161, 177 (2d Cir. 2005); *SEC v. Lucent Techs.*, 610 F.Supp.2d 342, 359–61 (D.N.J. 2009); *SEC v. KPMG LLP*, 412 F.Supp.2d 349, 377–78 (S.D.N.Y. 2006); *SEC v. PIMCO Advisors Fund Mgmt. LLC*, 341 F.Supp.2d 454, 467 (S.D.N.Y. 2004).

Permitting primary scheme liability to be imposed on Lorenzo based on statements he did not make would also significantly broaden the categories of defendants who can be targeted for primary liability. All of these newly at-risk defendants would be secondary actors at best. As the court explained in *PIMCO*, to permit scheme liability "to attach to individuals who did no more than facilitate preparation of material misrepresentations or omissions actually communicated by others ... would swallow the bright-line test between primary and secondary liability." 341 F.Supp.2d at 467; *see also Kelly*, 817 F.Supp.2d at 343.

The misconduct that the SEC alleged against Lorenzo involves no more than his facilitation of the distribution of misstatements that were made by others. To allow Lorenzo's ministerial conduct to serve as the basis for scheme liability would render the distinction between claims for misstatements and claims for fraudulent schemes meaningless.

Given the foregoing, allowing the finding that Lorenzo committed securities fraud to stand would be unjust and inconsistent with the carefully laid out structure of the antifraud provisions of the federal securities laws. Allowing the finding of liability to stand would also undermine this Court's holdings in *Janus* concerning the elements of a fraudulent statement claim and in *Central Bank* which addressed the important distinction between primary and secondary actors for purposes of securities fraud liability.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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January 26, 2018

APPENDIX

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APPENDIX A

UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 15-1202

[Filed September 29, 2017]

FRANCIS V. LORENZO, PETITIONER	)
	)
V.	)
	)
SECURITIES AND EXCHANGE COMMISSION, RESPONDENT	)

Argued September 15, 2016
Decided September 29, 2017

On Petition for Review of an Order of the Securities & Exchange Commission

Robert G. Heim argued the cause for petitioner. With him on the briefs were *Stephanie Rapp-Tully* and *Steven L. Herrick*.

Martin V. Totaro, Attorney, Securities and Exchange Commission, argued the cause for respondent. On the brief were *Anne K. Small*, General Counsel, *Michael A. Conley*, Solicitor, and *Benjamin L. Schiffrin*, Senior Litigation Counsel.

Before: GRIFFITH, KAVANAUGH, and SRINIVASAN, *Circuit Judges*.

Opinion for the Court filed by *Circuit Judge* SRINIVASAN.

Dissenting opinion filed by *Circuit Judge* KAVANAUGH.

SRINIVASAN, *Circuit Judge*: The Securities and Exchange Commission found that Francis Lorenzo sent email messages to investors containing misrepresentations about key features of a securities offering. The Commission determined that Lorenzo's conduct violated various securities-fraud provisions. We uphold the Commission's findings that the statements in Lorenzo's emails were false or misleading and that he possessed the requisite intent.

We cannot sustain, however, the Commission's determination that Lorenzo's conduct violated one of the provisions he was found to have infringed: Rule 10b-5(b). That rule bars the making of materially false statements in connection with the purchase or sale of securities. We conclude that Lorenzo did not "make" the false statements at issue for purposes of Rule 10b-5(b) because Lorenzo's boss, and not Lorenzo himself, retained "ultimate authority" over the statements. *Janus Capital Grp., Inc. v. First Derivative Traders*, 564 U.S. 135, 142 (2011).

While Lorenzo's boss, and not Lorenzo, thus was the "maker" of the false statements under Rule 10b-5(b), Lorenzo played an active role in perpetrating the fraud by folding the statements into emails he sent directly to investors in his capacity as director of investment banking, and by doing so with an intent to deceive. Lorenzo's conduct therefore infringed the other securities-fraud provisions he was charged with

violating. But because the Commission's choice of sanctions to impose against Lorenzo turned in some measure on its misimpression that his conduct violated Rule 10b-5(b), we set aside the sanctions and remand the matter to enable the Commission to reassess the appropriate penalties.

I.

A.

In February 2009, Francis Lorenzo became the director of investment banking at Charles Vista, LLC. Charles Vista was a registered broker-dealer owned by Gregg Lorenzo, no relation to Francis. (For clarity of reference, we will refer to Francis Lorenzo as "Lorenzo" and will use Gregg Lorenzo's first name when referring to him.)

Charles Vista's biggest client, and Lorenzo's only investment-banking client at the time, was a start-up company named Waste2Energy Holdings, Inc. (W2E). W2E claimed to have developed a "gasification" technology that could generate electricity by converting solid waste to gas. W2E's business model relied on the technology's living up to its potential. If it failed to do so, the great majority of W2E's assets—the "intangibles," in balance-sheet lingo—would have to be written off entirely.

W2E's conversion technology never materialized. In September 2009, W2E sought to escape financial ruin by offering up to $15 million in convertible debentures. (Debentures are "debt secured only by the debtor's earning power, not by a lien on any specific asset." BLACK'S LAW DICTIONARY 486 (10th ed. 2014)). Charles

Vista would serve as the exclusive placement agent for W2E's debenture offering.

W2E's most recent SEC filing at the time, its June 3, 2009 Form 8-K (used to notify investors of certain specified events), contained no indication of any possible devaluation of the company's intangible assets. Rather, the form stated that W2E's intangibles were worth just over $10 million as of the end of 2008. On September 9, 2009, W2E issued a Private Placement Memorandum as a guidebook for potential investors in the debentures. That guidebook, like the June 2009 Form 8-K, included no mention of any devaluation of the company's intangibles.

Following a lengthy audit, however, W2E changed its public tune. On October 1, 2009, the company filed an amended Form 8-K in which it reported a total "impairment" of its intangible assets because "management made a determination that the value of the assets acquired were of no value." J.A. 703. As of March 31, 2009, W2E now clarified, its gasification technology should have been valued at *zero*, and its total assets at only $370,552. On the same day it filed its amended Form 8-K, October 1, 2009, W2E also filed a quarterly Form 10-Q in which it valued its total assets at $660,408 as of June 30, 2009.

Later on October 1, Lorenzo's secretary alerted him (via email) about W2E's amended Form 8-K filing. The next day, Lorenzo emailed all Charles Vista brokers links to both of W2E's October 1 filings. On October 5, he received an email from W2E's Chief Financial Officer explaining the reasons for "[t]he accumulated deficit we have reported." *Id.* at 740. The CFO reiterated that W2E had written off "all of our

intangible assets . . . of about $11 million" due to "our assessment of the value of what those asset[s] are worth today." *Id.*

On October 14, Lorenzo separately emailed two potential investors "several key points" about W2E's pending debenture offering. *Id.* at 794, 796. His emails, however, omitted any mention of the wholesale devaluation of W2E's intangibles. On the contrary, Lorenzo's emails assured both recipients that the offering came with "3 layers of protection: (I) [W2E] has over $10 mm in confirmed assets; (II) [W2E] has purchase orders and LOI's for over $43 mm in orders; (III) Charles Vista has agreed to raise additional monies to repay these Debenture holders (if necessary)." *Id.* One of Lorenzo's messages said it had been sent "[a]t the request of Gregg Lorenzo," *id.* at 796, and the other stated it had been sent "[a]t the request of Adam Spero [a broker with Charles Vista] and Gregg Lorenzo," *id.* at 794. In both messages, Lorenzo urged the recipients to "[p]lease call [him] with any questions." *Id.* at 794, 796. And he signed both messages with his name and title as "Vice President – Investment Banking." *Id.*

B.

On February 15, 2013, the Commission commenced cease-and-desist proceedings against Lorenzo, Gregg Lorenzo, and Charles Vista. It charged each with violating three securities-fraud provisions: (i) Section 17(a)(1) of the Securities Act of 1933, 15 U.S.C. § 77q(a)(1); (ii) Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j; and (iii) Securities Exchange Act Rule 10b-5, 17 C.F.R. § 240.10b-5. Gregg Lorenzo and Charles Vista settled the charges against

them, but the claims against Lorenzo proceeded to resolution before the agency.

An administrative law judge concluded that Lorenzo had "willfully violated the antifraud provisions of the Securities and Exchange Acts by his material misrepresentations and omissions concerning W2E in the emails." *Gregg C. Lorenzo, Francis V. Lorenzo, and Charles Vista, LLC*, SEC Release No. 544, 107 SEC Docket 5934, 2013 WL 6858820, at *7 (Dec. 31, 2013). The ALJ deemed "[t]he falsity of the representations in the emails . . . staggering" and Lorenzo's mental state with respect to those misstatements at least "reckless." *Id.* As a result, the ALJ ordered Lorenzo to: (i) cease and desist from violating each securities-fraud provision giving rise to the charges against him; (ii) forever refrain from participating in the securities industry in several enumerated respects; and (iii) pay a civil monetary penalty of $15,000. *Id.* at *10.

Lorenzo petitioned the Commission for review. Following "an independent review of the record," the full Commission sustained the ALJ's decision, including her "imposition of an industry-wide bar, a cease-and-desist order, and a $15,000 civil penalty." *Francis V. Lorenzo*, SEC Release No. 9762, 111 SEC Docket 1761, 2015 WL 1927763, at *1 (Apr. 29, 2015) (*Lorenzo*). The Commission found that Lorenzo "knew each of [the emails' key statements] was false and/or misleading when he sent them." *Id.* It concluded that the sanctions were "in the public interest to deter Lorenzo and others in similar positions from committing future violations." *Id.* at *17. The Commission later denied Lorenzo's motion for reconsideration.

Lorenzo filed a timely petition for review in this court. He challenges only the Commission's imposition of an industry-wide bar and a $15,000 civil penalty, not the cease-and-desist order.

II.

We first consider Lorenzo's challenges to the Commission's findings that the relevant statements in his email messages were false or misleading and were made with the requisite mental state. The three pertinent statements are the three "layers of protection" enumerated in both of Lorenzo's October 14, 2009, email messages to potential investors about the debenture offering. Lorenzo challenges the Commission's determination that two of the three statements were false or misleading, and he also challenges the Commission's conclusion that he possessed the requisite intent with respect to all three of the statements.

With regard to his intent, establishing a violation of Section 17(a)(1) of the Securities Act, Section 10(b) of the Exchange Act, or Exchange Act Rule 10b-5 "requires proof of scienter." *Dolphin & Bradbury, Inc. v. SEC*, 512 F.3d 634, 639 (D.C. Cir. 2008). That standard in turn requires demonstrating "an intent to deceive, manipulate, or defraud." *Id.* (quoting *SEC v. Steadman*, 967 F.2d 636, 641 (D.C. Cir. 1992)). The scienter requirement can be satisfied by a showing of "[e]xtreme recklessness," which exists when "the danger was so obvious that the actor was aware of it and consciously disregarded it." *Id.*

The question whether Lorenzo acted with scienter, like the question whether the statements were false or

misleading, is a question of fact. *Id.* at 639. The Commission's "factual findings are conclusive if supported by substantial evidence." *Seghers v. SEC*, 548 F.3d 129, 132 (D.C. Cir. 2008). Although "[s]ubstantial evidence is more than a mere scintilla," *Kornman v. SEC*, 592 F.3d 173, 184 (D.C. Cir. 2010), we have repeatedly described the standard as a "very deferential" one, *e.g.*, *Siegel v. SEC*, 592 F.3d 147, 155 (D.C. Cir. 2010); *Dolphin & Bradbury*, 512 F.3d at 639; *Nat'l Ass'n of Sec. Dealers v. SEC*, 801 F.2d 1415, 1419 (D.C. Cir. 1986). Applying that standard here, we conclude that the Commission's findings as to falsity and scienter are supported by substantial evidence with regard to each of the three pertinent statements in Lorenzo's emails.

A.

The first of the three statements at issue advised potential investors that the "Company has over $10 mm in confirmed assets." J.A. 794, 796. Lorenzo does not directly dispute the falsity of that statement. Nor could he: by the time Lorenzo sent the October 14, 2009, email messages containing that statement, W2E had entirely written off its intangibles and disclosed that its remaining assets were worth far less than $1 million. And Lorenzo himself testified that W2E "would be lucky to get a million" for its intangibles after they had been marked down. *Id.* at 128.

As to the question of scienter, Lorenzo contends that, when he sent the emails, he held a good-faith belief that W2E had over $10 million in confirmed assets. The Commission concluded otherwise, and its finding of scienter is supported by substantial evidence.

One of Lorenzo's chief duties involved conducting due diligence on his clients, including reviewing their financial statements and public SEC filings. During the relevant time, W2E was Lorenzo's sole investment-banking client. He knew that W2E's financial situation was "horrible from the beginning" and that its gas-conversion technology had not worked as planned. *Id.* at 124. He also knew that he stood to gain seven to nine percent of any funds he raised from the debenture offering.

The record shows that, when Lorenzo viewed W2E's June 2009 Form 8-K, he disbelieved the Form's valuation of the company's intangible assets at $10 million. He agreed that the intangibles were a "dead asset" that would be "hugely discounted," *id.* at 127-28, and that W2E would be "lucky [to] get a million dollars for that asset," *id.* at 128-29. He also thought it significant that the $10 million valuation had not been audited, because without such scrutiny, "there is way too much risk for investors." *Id.* at 126. He acknowledged that he had warned Gregg Lorenzo as early as April 2009 to refrain from collateralizing a debenture offering with W2E's intangibles, because those assets "provided no protection" to investors. *Id.* at 159. Lorenzo understood that, if a default occurred, "clients would not be able to recoup their money based on a liquidation of this asset." *Id.* He instead viewed the debenture offering as a "toxic convertible debt spiral." *Lorenzo*, 2015 WL 1927763, at *5.

Evidence concerning Lorenzo's state of mind can also be gleaned from his actions in helping prepare Charles Vista's Private Placement Memorandum for the debenture offering. On August 26, 2009, he asked

W2E's principals to value the company's intangibles at $10 million in the upcoming Memorandum. He received no response. He broached the subject again on September 1, this time leaving the intangibles' value blank, because he "w[asn't] sure what [it] was worth anymore." J.A. 135, 739. The final Memorandum assigned no concrete value to W2E's intangibles; it instead divulged that the company had experienced "significant operating losses" and did "not expect to be profitable for at least the foreseeable future." *Lorenzo*, 2015 WL 1927763, at *3.

In its October 1 SEC filings, W2E publicly disclosed the wholesale write-off of its intangibles. It did so in a tri-column chart entitled "Goodwill and Technology," and it followed that numerical presentation with a textual explanation for the mark-down. Lorenzo acknowledged that he read the amended Form 8-K on October 1 (although, according to him, "[p]robably not as closely as I should have"). J.A. 140. And he received an email from W2E's CFO on October 5 succinctly contextualizing the massive devaluation of W2E's intangible assets.

The evidence therefore supports concluding that, at least by October 5, Lorenzo knew that W2E's intangibles were valueless. He gave testimony on the issue as follows: "Q. So it is fair to say . . . that on October 5, 200[9], you were aware that the $10 million asset had been written off by [W2E]. Correct? A. Okay. I will agree to that. That's correct. Q. That is a fair statement? A. Yes." *Id.* at 151. That admission is difficult to reconcile with Lorenzo's statement that he "unintentional[ly] miss[ed]" the import of the October 5 email. *Id.* at 148. The Commission justifiably credited

his more inculpatory rendition of events, especially in light of his broader, scienter-related concession: "Q. [D]id you know that those statements were inaccurate and misleading? A. Yes. Q. You knew at the time? A. At the time? I can't sit here and say that I didn't know." *Id.* at 158.

According to the Commission, "[t]hat Lorenzo could have looked at [W2E's] filings, which was his job, and missed what was one of the most pertinent facts in them—the valuation of the company's assets—is either untrue or extreme recklessness." *Lorenzo*, 2015 WL 1927763, at *9. The Commission considered it "at least extremely reckless" for Lorenzo to have sent email messages claiming that W2E had over $10 million in "confirmed" assets, given his "long-standing concern about the legitimacy" of those assets. *Id.* We perceive no basis for setting aside the Commission's conclusions as unsupported by substantial evidence.

In resisting that conclusion, Lorenzo relies in part on a $14 million valuation of W2E's assets in a W2E research report emailed by Charles Vista's Chief Compliance Officer to the firm's brokers on the same day Lorenzo sent his pertinent emails (October 14, 2009). The Commission sensibly reasoned that "the mere fact that, for whatever unknown reason, a compliance officer sent an inaccurate research report internally to the firm's brokers is neither analogous to, nor an excuse for, Lorenzo's knowingly sending misleading emails to prospective investors." *Id.* at *9 n.23.

B.

The second contested statement is the assertion in Lorenzo's emails that "[t]he Company has purchase orders and LOI's for over $43 mm in orders." J.A. 794, 796. He maintains that the Commission erred in deeming that statement false or misleading. He notes that, at one point, Charles Vista did in fact receive a $43 million letter of intent from a potential customer in the Caribbean, and that W2E's CEO "put a lot of confidence" in such letters. *Id.* at 160. But as the Commission rightly notes, the Caribbean letter did not obligate its drafter to do anything, and the transaction proceeded no further. By the time Lorenzo sent his emails on October 14, 2009, W2E had no outstanding purchase orders. Lorenzo's emails nonetheless assured the recipients that W2E had over $43 million in "purchase orders *and* LOI's." The Commission thus was fully justified in finding that statement false or misleading. *See Lorenzo*, 2015 WL 1927763, at *6.

Lorenzo also disputes the Commission's finding of scienter concerning the extent of W2E's anticipated cash flow. Asked whether he knew at the time that the $43 million figure was misleading, Lorenzo testified as follows: "I can't say that with a hundred percent because they did have LOI's for 43 million." J.A. 160. As his other testimony revealed, however, Lorenzo understood that W2E's sole letter of intent was "non-binding," a mere potentiality that the company "hoped would materialize." *Id.* at 162. And by September 2009, he "didn't think that the 43 million LOI was ever going to turn into purchases." *Id.* at 164. Lorenzo testified repeatedly to that effect. *See id.* at 163-64 ("Q. And by September 2009 you didn't think it was ever going to

come through, right? A. . . . That is correct."); *id.* at 164 ("Q. So sometime in September you lost confidence that this 43 million was ever going to happen? A. Yes.").

The clear implication of the statement in Lorenzo's email messages was that W2E anticipated a $43 million influx of capital from past and future orders. Yet the record reveals grave doubts on Lorenzo's part that "$43 mm in orders" (or *any* orders) would actually occur. Substantial evidence therefore supports the Commission's finding of scienter as to that statement.

C.

The third statement at issue is the assertion in Lorenzo's email messages that "Charles Vista has agreed to raise additional monies to repay these Debenture holders (if necessary)." *Id.* at 794, 796. Lorenzo disputes the Commission's conclusion that the statement was false or misleading. He contends that Gregg Lorenzo could have made such an agreement for Charles Vista, had done so on prior occasions for debenture holders, and had allegedly met with additional brokers about raising funds for W2E. The Commission permissibly regarded those assertions as "establish[ing] only the theoretical possibility that Charles Vista could have raised additional money to repay investors, not that it had agreed to do so (as Lorenzo's emails claimed)." *Lorenzo*, 2015 WL 1927763, at *7.

With regard to scienter, Lorenzo observes that the Commission included no specific citations to the record in support of its finding. It is true that, although the Commission quoted the evidentiary record at length, it did not cite the particular page numbers on which

certain arguments and quotations appeared. But we "uphold a decision of less than ideal clarity if the agency's path may reasonably be discerned." *Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983) (quoting *Bowman Transp., Inc. v. Arkansas-Best Freight Sys.*, 419 U.S. 281, 286 (1974)). That standard is readily satisfied here.

Lorenzo allowed, at least in hindsight, that "you can interpret this [statement] as being misleading." J.A. 167. Moreover, according to his own testimony, at the time he sent the emails, he did not believe Charles Vista could raise enough money to repay debenture holders. For instance, he testified that, as of October 2009, "it is accurate to say that Charles Vista would not have the buying power or the resources to properly fund [W2E] in order to repay the debentures." *Id.* at 172. Given Lorenzo's knowledge that Charles Vista could not have repaid debenture holders, the Commission could certainly conclude that Lorenzo believed that no such agreement existed. As a result, substantial evidence supports the Commission's finding that Lorenzo acted with scienter with regard to the assurance to investors that Charles Vista had made such a promise.

III.

The Commission found that Lorenzo's actions in connection with his email messages violated Section (17)(a)(1) of the Securities Act and Section 10(b) of the Exchange Act, as implemented by the Commission's Rule 10b-5. The Rule contains three subsections, and the Commission concluded that Lorenzo had violated all three.

We now consider Lorenzo's argument that he did not "make" the relevant statements within the meaning of the express terms of one of Rule 10b-5's subsections, Rule 10b-5(b). We agree with Lorenzo that, under the Supreme Court's decision in *Janus Capital Group, Inc. v. First Derivative Traders*, 564 U.S. 135 (2011), he did not "make" the statements at issue for purposes of Rule 10b-5(b). Even so, we conclude that his status as a non-"maker" of the statements under Rule 10b-5(b) does not vitiate the Commission's conclusion that his actions violated the other subsections of Rule 10b-5, as well as Section 17(a)(1).

A.

Under Rule 10b-5(b), it is unlawful to "make any untrue statement of a material fact . . . in connection with the purchase or sale of any security." 17 C.F.R. § 240.10b-5(b). In *Janus*, the Supreme Court explained what it means to "make" a statement within the meaning of that prohibition:

> For purposes of Rule 10b-5, the maker of a statement is the person or entity with ultimate authority over the statement, including its content and whether and how to communicate it. Without control, a person or entity can merely suggest what to say, not "make" a statement in its own right. One who prepares or publishes a statement on behalf of another is not its maker.

564 U.S. at 142. "[I]n the ordinary case," the Court continued, "attribution within a statement or implicit from surrounding circumstances is strong evidence that a statement was made by—and only by—the party to whom it is attributed." *Id.* at 142-43.

The *Janus* Court held that an investment adviser that had assisted in preparing a mutual fund's prospectuses did not "make" the statements contained therein, because the adviser lacked "ultimate control" over the statements' content and dissemination. *Id.* at 148. The investment adviser had merely "participate[d] in the drafting of a false statement"—"an undisclosed act preceding the decision of an independent entity to make a public statement." *Id.* at 145. The Court illustrated the operation of its test through the following analogy: "Even when a speechwriter drafts a speech, the content is entirely within the control of the person who delivers it. And it is the speaker who takes credit—or blame—for what is ultimately said." *Id.* at 143.

Under the *Janus* test, a person cannot have "made" a statement if he lacked ultimate authority over what it said and whether it was said, including if he prepared or published it on behalf of another. In light of that understanding, we find that Lorenzo was not the "maker" of the pertinent statements set out in the email messages he sent to potential investors, even viewing the record in the light most favorable to the Commission.

Lorenzo contends that he sent the email messages at the behest of his boss, Gregg Lorenzo, and that Gregg Lorenzo supplied the content of the false statements, which Lorenzo copied and pasted into the messages before distributing them. As a result, Lorenzo contends, Gregg Lorenzo (and not Lorenzo himself) was the "maker" of the statements under *Janus*. The Commission found otherwise, concluding that Lorenzo "was ultimately responsible for the emails' content and

dissemination." *Lorenzo*, 2015 WL 1927763, at *10. We cannot sustain the Commission's conclusion that Lorenzo had "ultimate authority" over the false statements under *Janus*. 564 U.S. at 142. Gregg Lorenzo, and not Lorenzo, retained ultimate authority.

Voluminous testimony established that Lorenzo transmitted statements devised by Gregg Lorenzo at Gregg Lorenzo's direction. For instance, Lorenzo said: "I cut and paste[d] an e-mail and sent it to [investors]," J.A. 153; "I was asked to send these e-mails out by Gregg Lorenzo," *id.* at 156; and "I cut and pasted and sent it," *id.* at 157. He also stated: "I remember getting—getting the e-mail address from [Gregg Lorenzo] and then cut and past[ed] this—this thing and sent it," *id.* at 199; "[Gregg Lorenzo] gave me the e-mail address, I typed it into the 'to' column and cut and pasted this—the content and sent it out," *id.*; "My boss asked me to send these e-mails out and I sent them out," *id.* at 200; "[I] sent these e-mails out at the request of my superior," *id.* at 208; and "I simply was asked to send the e-mail out," *id.* at 208-09.

In the face of that consistent testimony, the Commission anchored its conclusion almost entirely in the following remark from Lorenzo: "If memory serves me—I think I authored it and then it was approved by Gregg and Mike [Molinaro, Charles Vista's Chief Compliance Officer]." J.A. 155. That assertion, even apart from its equivocation, must be read alongside the rest of Lorenzo's testimony. Immediately before and after uttering that line, Lorenzo explained that "I cut and paste[d] an e-mail and sent it" and "I cut and pasted and sent it." *Id.* at 153, 157. And he consistently testified to the same effect throughout. In that light,

Lorenzo's remark that he "authored" the emails cannot bear the weight given it by the Commission. Rather, the statement is fully consistent with Lorenzo's repeated account that, while he produced the email messages for final distribution from himself to the investors—and in that sense "authored" the messages—he populated the messages with content sent by Gregg Lorenzo.

In the line of testimony on which the Commission relies, moreover, Lorenzo stated that, before he sent the messages, they were "approved" by Gregg Lorenzo. That observation reinforces Gregg Lorenzo's ultimate authority over the substance and distribution of the emails: Gregg Lorenzo asked Lorenzo to send the emails, supplied the central content, and approved the messages for distribution. To be sure, Lorenzo played an active role in perpetrating the fraud by producing the emails containing the false statements and sending them from his account in his capacity as director of investment banking (and doing so with scienter). But under the test set forth in *Janus*, Gregg Lorenzo, and not Lorenzo, was "the maker" of the false statements in the emails. 564 U.S. at 142.

The Commission's remaining observations do not alter our conclusion. For instance, the Commission noted that Lorenzo "put his own name and direct phone number at the end of the emails, and he sent the emails from his own account." *Lorenzo*, 2015 WL 1927763, at *10. That sort of signature line, however, can often exist when one person sends an email that "publishes a statement on behalf of another," with the latter person retaining "ultimate authority over the statement." *Janus*, 564 U.S. at 142.

The Commission also referenced Lorenzo's testimony that "he did not recall ever discussing either of the emails or their subject matter with Gregg Lorenzo." *Lorenzo*, 2015 WL 1927763, at *10. That comment, however, is consistent with the understanding that Lorenzo played a minimal role in devising the emails' false statements. And although the email messages said that the Investment Banking Division—which Lorenzo headed—was "summariz[ing] several key points" about the debenture offering, J.A. 794, 796, the content of those points evidently had been supplied by Gregg Lorenzo. The emails, moreover, began by stating that they were being sent at Gregg Lorenzo's request. Lorenzo testified elsewhere that Gregg Lorenzo had remarked, "I want this [to] come from our investment banking division. Can you send this out for me?" *Id.* at 217.

Under the Supreme Court's decision in *Janus*, in short, Lorenzo cannot be considered to have been "the maker" of the statements in question for purposes of Rule 10b-5(b)—i.e., "the person . . . with ultimate authority" over them. 564 U.S. at 142. That person was Gregg Lorenzo, and not (or not also) Lorenzo.

B.

Lorenzo next argues that, if he was not "the maker" of the false statements at issue within the meaning of Rule 10b-5(b), his conduct necessarily also falls outside the prohibitions of Exchange Act Section 10(b), Rules 10b-5(a) and (c), and Securities Act Section 17(a)(1). The Commission concluded otherwise, incorporating by reference its reasoning in *John P. Flannery & James D. Hopkins*, SEC Release No. 3981, 110 SEC Docket 2463, 2014 WL 7145625 (Dec. 15, 2014), *vacated*, *Flannery v.*

SEC, 810 F.3d 1 (1st Cir. 2015) (rejecting the Commission's key factual determinations on substantial-evidence grounds). The Commission determined that, "[i]ndependently of whether Lorenzo's involvement in the emails amounted to 'making' the misstatements for purposes of Rule 10b-5(b), he knowingly sent materially misleading language from his own email account to prospective investors," thereby violating those other provisions. *Lorenzo*, 2015 WL 1927763, at *11.

We sustain the Commission's conclusion to that effect. At least in the circumstances of this case, in which Lorenzo produced email messages containing false statements and sent them directly to potential investors expressly in his capacity as head of the Investment Banking Division—and did so with scienter—he can be found to have infringed Section 10(b), Rules 10b-5(a) and (c), and Section 17(a)(1), regardless of whether he was the "maker" of the false statements for purposes of Rule 10b-5(b).

1. Rules 10b-5(a) and (c), along with Sections 10(b) and 17(a)(1)—all unlike Rule 10b-5(b)—do not speak in terms of an individual's "making" a false statement. Indeed, "[t]o make any . . . statement" was the critical language construed in *Janus*: what the Court described as the "phrase at issue." 564 U.S. at 142 (alteration in original) (quoting 17 C.F.R. § 240.10b-5(b)). That language appears in Rule 10b-5(b), but not in the other provisions Lorenzo was found to have violated.

In particular, Rule 10b-5(a) prohibits "employ[ing] any device, scheme, or artifice to defraud . . . in connection with the purchase or sale of any security." 17 C.F.R. § 240.10b-5(a). And Rule 10b-5(c) bars

"engag[ing] in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person . . . in connection with the purchase or sale of any security." *Id.* § 240.10b-5(c). Consequently, Rule 10b-5(b) "specifies the making of an untrue statement of a material fact and the omission to state a material fact. The first and third subparagraphs are not so restricted." *Affiliated Ute Citizens of Utah v. United States*, 406 U.S. 128, 152-53 (1972).

Nor are Securities Act Section 17(a)(1) and Exchange Act Section 10(b). Section 17(a)(1) makes it unlawful "to employ any device, scheme, or artifice to defraud" in offering or selling a security. 15 U.S.C. § 77q(a)(1). And Section 10(b) forbids "us[ing] or employ[ing] . . . any manipulative or deceptive device or contrivance" in contravention of rules prescribed by the Commission. 15 U.S.C. § 78j(b).

Here, Lorenzo, acting with scienter (i.e., an intent to deceive or defraud, or extreme recklessness to that effect), produced email messages containing three false statements about a pending offering, sent the messages directly to potential investors, and encouraged them to contact him personally with any questions. Although Lorenzo does not qualify as the "maker" of those statements under *Janus* because he lacked ultimate authority over their content and dissemination, his own active "role in producing and sending the emails constituted employing a deceptive 'device,' 'act,' or 'artifice to defraud' for purposes of liability under Section 10(b), Rule 10b-5(a) and (c), and Section 17(a)(1)." *Lorenzo*, 2015 WL 1927763, at *11.

Lorenzo's conduct fits comfortably within the ordinary understanding of those terms. Indeed, he

presents no argument that his actions fail to satisfy the statutory and regulatory language. He does not examine—or even reference—the text of those provisions in arguing that they should be deemed not to apply to his conduct.

Lorenzo does not contend before us, for instance, that he simply passed along information supplied by Gregg Lorenzo without pausing to think about the truth or falsity of what he was sending to investors. If those were the facts, he might attempt to argue that he cannot be considered to have "employed" any fraudulent device or artifice, or "engaged" in any fraudulent or deceitful act, within the meaning of Rules 10b-5(a) and (c), and of Sections 10(b) and 17(a)(1). But while Lorenzo argued before the Commission that he produced and sent the emails at Gregg Lorenzo's request without giving them thought, the Commission found "implausible" any suggestion that he merely passed along the messages in his own name without thinking about their content. *Lorenzo*, 2015 WL 1927763, at *9. Lorenzo does not challenge that finding here.

We therefore consider the case on the understanding that Lorenzo, having taken stock of the emails' content and having formed the requisite intent to deceive, conveyed materially false information to prospective investors about a pending securities offering backed by the weight of his office as director of investment banking. On that understanding, the language of Sections 10(b) and 17(a)(1), and of Rules 10b-5(a) and (c), readily encompasses Lorenzo's actions.

2. Instead of presenting any argument that his conduct falls outside the language of those provisions,

Lorenzo asserts that, if he could be found to have violated the provisions, the decision in *Janus* would effectively be rendered meaningless. *See SEC v. Kelly*, 817 F. Supp. 2d 340, 344 (S.D.N.Y. 2011). He notes the *Janus* Court's interest in interpreting the term "make" in a manner that would avoid undermining the Court's previous holding that private actions under Rule 10b-5 cannot be premised on conceptions of secondary (i.e., aiding-and-abetting) liability. *See Janus*, 564 U.S. at 143 (discussing *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164 (1994)).

As the Court explained in *Janus*, whereas the Commission can bring actions under Rule 10b-5 based on an aiding-and-abetting theory, private parties—after *Central Bank*—cannot. *Id.* The *Janus* Court reasoned that a "broader reading of 'make,'" encompassing "persons or entities without ultimate control over the content of a statement," could mean that "aiders and abettors would be almost nonexistent." *Id.* That result, the Court believed, would have undercut an implicit understanding from *Central Bank*: that "there must be some distinction between those who are primarily liable . . . and those who are secondarily liable." *Id.* at 143 n.6. The same considerations, Lorenzo contends, should weigh in favor of concluding that his conduct did not violate Section 10(b), Rules 10b-5(a) and (c), and Section 17(a)(1). We are unpersuaded.

To the extent the *Janus* Court's concerns about aiding-and-abetting liability in private actions under Rule 10b-5(b) should inform our interpretation of those other four provisions, the conduct at issue in *Janus* materially differs from Lorenzo's actions in this case.

Janus involved an investment adviser that initially drafted false statements which an independent entity subsequently decided to disseminate to investors in its own name. The investment adviser's role in originally devising the statements was unknown to the investors who ultimately received them. The Court thus described the investment adviser's conduct as "an undisclosed act preceding the decision of an independent entity to make a public statement." 564 U.S. at 145.

In this case, by contrast, Lorenzo's role was not "undisclosed" to investors. The recipients were fully alerted to his involvement: Lorenzo sent the emails from his account and under his name, in his capacity as director of investment banking at Charles Vista. While Gregg Lorenzo supplied the content of the false statements for inclusion in Lorenzo's email messages, Lorenzo effectively vouched for the emails' contents and put his reputation on the line by listing his personal phone number and inviting the recipients to "call with any questions." J.A. 794, 796. Nor did the dissemination of the false statements to investors result only from the separate "decision of an independent entity." *Janus*, 564 U.S. at 145. Lorenzo himself communicated with investors, directly emailing them misstatements about the debenture offering.

Unlike in *Janus*, therefore, the recipients of Lorenzo's emails were not exposed to the false information only through the intervening act of "another person." *Id.* For the same reasons, Lorenzo's conduct also differs from the actions considered in *Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc.*, 552 U.S. 148 (2008). There, the Supreme

Court held that parties who allegedly played a role in a scheme to make false statements to investors could not be held liable in a private action under Rule 10b-5. The Court explained that the parties' acts "were not disclosed to the investing public" and they "had no role" in "disseminating" the misstatements in question. *Id.* at 155, 161. Lorenzo, unlike the defendants in *Janus* and *Stoneridge*, transmitted misinformation directly to investors, and his involvement was transparent to them.

As a result, insofar as the *Janus* Court declined to bring the investment adviser's actions in that case within the fold of Rule 10b-5 because doing so might reach too many persons fairly considered to be aiders and abettors, the same is not true of Lorenzo's distinct conduct in this case. The Court's concern that "aiders and abettors would be almost nonexistent" if a private action under Rule 10b-5 reached "an undisclosed act preceding the decision of an independent entity to make a public statement," *Janus*, 564 U.S. at 143, 145, need not obtain in the case of a person's self-attributed communications sent directly to investors (and backed by scienter). Lorenzo's actions thus can form the basis of a violation of Rules 10b-5(a) and (c) (as well as Sections 10(b) and 17(a)(1)) while still leaving ample room for "distinction between those who are primarily liable . . . and those who are secondarily liable." *Id.* at 143 n.6; *see Stoneridge*, 552 U.S. at 166 ("[T]he implied right of action in § 10(b) continues to cover secondary actors who commit primary violations." (citing *Central Bank*, 511 U.S. at 191)).

3. Lorenzo intimates more broadly that actions involving false statements must fit within Rule 10b-

5(b) and cannot be brought separately under Rules 10b-5(a) or (c) (or Section 17(a)(1)). We know of no blanket reason, however, to treat the various provisions as occupying mutually exclusive territory, such that false-statement cases must reside exclusively within the province of Rule 10b-5(b). And any suggestion that the coverage of Rule 10b-5(b) must be distinct from that of Rules 10b-5(a) and (c) presumably would mean that each of the latter two provisions likewise must occupy entirely separate ground from one another. In our view, however, the provisions' coverage may overlap in certain respects.

Significantly, the Supreme Court recently described Rule 10b-5 in a manner confirming that conduct potentially subject to Rule 10b-5(b)'s bar against making false statements can also fall within Rule 10b-5(a)'s more general prohibition against employing fraudulent devices: the Court explained that "Rule 10b-5 . . . forbids the use of any 'device, scheme, or artifice to defraud' (*including* the making of any 'untrue statement of material fact' or any similar 'omi[ssion]')." *Chadbourne & Parke LLP v. Troice*, 134 S. Ct. 1058, 1063 (2014) (emphasis added).

The Court has also held that, although Section 14 of the Exchange Act establishes "a complex regulatory scheme covering proxy solicitations," the inapplicability of Section 14 to false statements in proxy materials does not preclude the application of Rule 10b-5 to the same statements. *SEC v. Nat'l Sec., Inc.*, 393 U.S. 453, 468 (1969). "The fact that there may well be some overlap is neither unusual nor unfortunate," the Court explained. *Id.* Here, correspondingly, Rules 10b-5(a) and (c), as well as Sections 10(b) and 17(a)(1), may

encompass certain conduct involving the dissemination of false statements even if the same conduct lies beyond the reach of Rule 10b-5(b).

In accordance with that understanding, a number of decisions have held that securities-fraud allegations involving misstatements can give rise to liability under related provisions even if the conduct in question does not amount to "making" a statement under *Janus*. *See, e.g.*, *SEC v. Big Apple Consulting USA, Inc.*, 783 F.3d 786, 795-96 (11th Cir. 2015); *SEC v. Monterosso*, 756 F.3d 1326, 1334 (11th Cir. 2014); *SEC v. Benger*, 931 F. Supp. 2d 904, 905-06 (N.D. Ill. 2013); *SEC v. Familant*, 910 F. Supp. 2d 83, 93-95 (D.D.C. 2012); *SEC v. Stoker*, 865 F. Supp. 2d 457, 464-65 (S.D.N.Y. 2012). We reach the same conclusion here with respect to the role played by Lorenzo in disseminating the false statements in his email messages to investors.

4. Our dissenting colleague would find that Lorenzo's actions did not violate Rules 10b-5(a) or (c), or Sections 10(b) or 17(a)(1). He advances two reasons for reaching that conclusion, each of which, in our respectful view, is misconceived.

a. The dissent's central submission is that Lorenzo acted without any intent to deceive or defraud. As our colleague sees things, Lorenzo simply transmitted false statements supplied by Gregg Lorenzo without giving any thought to their content. *See infra* at 1, 6 (Kavanaugh, J., dissenting). And Lorenzo ostensibly paid no attention to the content of the statements he sent even though: he included the statements in messages he produced for distribution from his own email account; he sent the statements in his name and capacity as investment banking director; and he

encouraged the recipients to contact him personally with questions about the content. Under our colleague's understanding, that is, Lorenzo offered to answer any questions about his emails even though he had supposedly paid no attention to what they said.

In adopting that understanding, the dissent relies on a finding by the ALJ that Lorenzo sent the emails without thinking about their contents. But the Commission, as we have noted, rejected the ALJ's conclusion to that effect as "implausible" in the circumstances. *Lorenzo*, 2015 WL 1927763, at *9. In our colleague's view, the court should accept the ALJ's finding, notwithstanding the Commission's rejection of it, because the ALJ could assess Lorenzo's credibility as a witness.

The dissent's (and ALJ's) factual understanding, however, is contradicted by Lorenzo's own account of his mental state to this court. Lorenzo raises no challenge to the Commission's rejection of any notion that he paid no heed to his messages' content. What is more, his argument on the issue of scienter rests on his affirmative contemplation—indeed, his ratification—of the content of his emails.

Unlike in his arguments before the ALJ and Commission, Lorenzo, in this court, does not take the position that he simply passed along statements supplied by Gregg Lorenzo without thinking about them. Such a suggestion appears nowhere in his briefing. To the contrary, he argues that, "[a]t the time the email was sent [he] *believed the statements to be true* and he did not act with scienter." Pet'r Reply Br. 6 (emphasis added). He further asserts that he "*had a good faith belief in the veracity of the statements*

contained in the email that was drafted by Gregg Lorenzo." Pet'r Opening Br. 18 (emphasis added); *id.* at 22 ("Petitioner had a good faith belief in the accuracy of the statements contained in the email."). He then attempts to explain why he could have believed the truth of the materially misleading statements contained in his email messages, arguments that we have already rejected in affirming the Commission's findings of scienter. *See supra* Part II.

For present purposes, what matters is that a person cannot have "believed statements to be true" at the time he sent them, or possessed a "good faith belief in their veracity," if he had given no thought to their content in the first place. In that light, our dissenting colleague relies on an account of Lorenzo's state of mind that stands in opposition to Lorenzo's account to us of his own state of mind. (As for our colleague's theory that Lorenzo could have formed a belief about the statements' truthfulness without even reading them, based purely on his trust of Gregg Lorenzo, *see infra* at 7 n.1 (Kavanaugh, J., dissenting), even if we assume that theory were viable as a conceptual matter, Lorenzo's arguments to us about his belief in the statements' truth rest solely on their content, not on any trust-without-verifying level of confidence in Gregg Lorenzo's veracity. Indeed, he testified that, at least as of November 2009, "there is no way on God's green earth [he] thought Gregg Lorenzo was an honest guy." J.A. 176.)

Perhaps Lorenzo concluded he could not overcome the Commission's assessment that it would be implausible to suppose he had blinded himself to the statements' content before sending them to investors

and offering to answer any questions about them. Or perhaps he determined that, insofar as he did so, he would have difficulty denying that he had acted with extreme recklessness—and therefore with scienter—in any event. Regardless, Lorenzo now takes the position that he took stock of the content of the statements, so much so that he formed a belief as to their truthfulness. And we are in no position to embrace an understanding of Lorenzo's mental state that is disclaimed by Lorenzo himself.

To be clear, the point here is not that Lorenzo failed to preserve an argument about scienter. Lorenzo devoted considerable attention to the issue of scienter in his briefing. But Lorenzo's arguments on the issue contain no suggestion that he sent his emails without giving thought to their contents. He instead contends he *did* think about the contents (and reasonably believed them to be truthful). In those circumstances, we do not so much defer to the *Commission*'s assessment of Lorenzo's state of mind over the ALJ's finding that Lorenzo gave no thought to his emails' content. Rather, we accede to *Lorenzo*'s account of his own mental state, which is incompatible with the finding of the ALJ.

But what if Lorenzo in fact had sought to argue to us, in concert with the ALJ's finding, that he gave no thought to the content of his email messages when sending them? In that event—which, again, is not the situation we face—the issue for us would have been whether the Commission's contrary conclusion is supported by substantial evidence, not whether the Commission or the ALJ has the better of the dispute between them on the matter. *See, e.g.*, *Kay v. FCC*, 396

F.3d 1184, 1189 (D.C. Cir. 2005); *Swan Creek Communications, Inc. v. FCC*, 39 F.3d 1217, 1221 (D.C. Cir. 1994); *see also Universal Camera Corp. v. NLRB*, 340 U.S. 474, 496 (1951).

The Commission's finding meets the deferential, substantial-evidence standard. After all, Lorenzo's emails marked the only time he communicated directly with prospective investors, the emails concerned a securities offering by his sole investment banking client, the emails said he would personally answer questions about their content, and the emails carried his professional imprimatur as director of investment banking—all of which support the Commission's rejection of the idea that Lorenzo simply sent his emails without taking any stock of what they said.

b. Even accepting that Lorenzo thought about the statements in his emails and sent them with an intent to deceive, the dissent would still conclude that Lorenzo's conduct falls outside the ambit of Rules 10b-5(a) and (c), and Sections 10(b) and 17(a)(1). *See infra* at 9 (Kavanaugh, J., dissenting). Our colleague grounds that conclusion in his agreement with the proposition put forward by certain other courts of appeals to the effect that "scheme liability"—i.e., the conduct prohibited by Rules 10b-5(a) and (c)—requires something more than false or misleading statements. *See Pub. Pension Fund Grp. v. KV Pharma. Co.*, 679 F.3d 972, 987 (8th Cir. 2012); *WPP Luxembourg Gamma Three Sari v. Spot Runner, Inc.*, 655 F.3d 1039, 1057-58 (9th Cir. 2011); *Lentell v. Merill Lynch & Co.*, 396 F.3d 161, 177 (2d Cir. 2005).

Our colleague appears to read those decisions' embrace of that proposition to rest on the need to

maintain a distinction between primary liability and secondary liability under Rule 10b-5. We have described the *Janus* Court's reliance on that concern and explained our conclusion that it does not carry the day in the specific circumstances of Lorenzo's conduct. *See supra* Part III.B.2.

Moreover, we do not read the referenced courts of appeals' decisions to rest on concerns about preserving a distinction between primary and secondary liability. None of those decisions discusses (or mentions) the concepts of primary and secondary liability or any need to maintain a separation between them. Indeed, two of the three decisions postdate *Janus*, yet neither cites *Janus*, much less invokes *Janus*'s concerns with construing the scope of Rule 10b-5(b) in a manner that would encompass too many aiders-and-abettors.

In addition, it is far from clear that the rule articulated by those decisions could suitably be grounded in concerns with preserving a distinction between primary and secondary liability. According to the decisions, a "defendant may only be liable as part of a fraudulent scheme based upon misrepresentations and omissions under Rules 10b-5(a) or (c) when the scheme also encompasses conduct beyond those misrepresentations or omissions." *WPP Luxembourg*, 655 F.3d at 1057; *see KV Pharma.*, 679 F.3d at 987; *Lentell*, 396 F.3d at 177. That understanding would be overinclusive if the objective in fact were to assure that aiders-and-abettors are not held primarily liable under those provisions.

Consider, for instance, the facts of *WPP Luxembourg*. There, the plaintiffs alleged sufficient facts to make out a claim of materially misleading

omissions under Rule 10b-5(b). 655 F.3d at 1051. There was no question that the defendants faced primary (not secondary) liability if the facts as pleaded were proved. *Id.* Yet the court held that the defendants could not be liable under Rules 10b-5(a) or (c) because there were no allegations against them apart from misstatements or omissions. *Id.* at 1057-58. The court's requirement that plaintiffs prove more than misstatements thus barred liability under those provisions even though there could have been no concerns about blurring the distinction between primary and secondary liability. Perhaps it is unsurprising, then, that, while Lorenzo relies on the importance of maintaining the primary-secondary liability distinction, he makes no reference to *WPP Luxembourg* or the other two decisions in his briefing.

For those reasons, we disagree with our dissenting colleague's suggestion that our holding conflicts with those decisions with regard to the primary-secondary liability distinction. *See infra* at 9 (Kavanaugh, J., dissenting). We do not understand those decisions to turn on that distinction.

Those decisions do generally state, however, that Rules 10b-5(a) and (c) require something more than misstatements. But they did not have occasion to elaborate on that understanding to any significant extent—including, importantly for purposes of this case, whether the same interpretation would extend to Section 17(a)(1). Insofar as those courts of appeals would find Lorenzo's actions to lie beyond the reach of those provisions, we read the provisions differently. Lorenzo's particular conduct, as we have explained, fits comfortably within the language of Rules 10b-5(a) and (c), along with that of Sections 10(b) and 17(a)(1).

Finally, we briefly respond to our dissenting colleague's belief that there is an incongruity in deciding both that Lorenzo was not a maker of the false statements under Rule 10b-5(b) and that he nonetheless employed a fraudulent device and engaged in a fraudulent act under Rules 10b-5(a) and (c) and Section 17(a)(1). *See infra* at 11 (Kavanaugh, J., dissenting). Those combined decisions, in our view, follow naturally from the terms of the provisions. Lorenzo was not the "maker" of the false statements because he lacked ultimate authority over them. Still, he "engaged" in a fraudulent "act" and "employed" a fraudulent "device" when, with knowledge of the statements' falsity and an intent to deceive, he sent the statements to potential investors carrying his stamp of approval as investment banking director. One can readily imagine persons whose ministerial acts in connection with false statements would fail to qualify either as "making" the statements or as "employing" any fraudulent device. Lorenzo, in our view, is not such a person.

IV.

Lorenzo's final challenge concerns the sanctions imposed against him. The Commission permanently barred Lorenzo "from association with any broker, dealer, investment adviser, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization and from participating in an offering of penny stocks." *Lorenzo*, 2015 WL 1927763, at *17. The Commission also ordered him to pay a $15,000 monetary penalty. Lorenzo argues that those penalties are arbitrary and capricious for various reasons, including that they are

disproportional to the severity of his misconduct and to the sanctions imposed in similar cases.

We decline to reach the merits of Lorenzo's challenges. The Commission chose the level of sanctions based in part on a misimpression that Lorenzo was the "maker" of false statements in violation of Rule 10b-5(b). Because we have now overturned the Commission's finding of liability under Rule 10b-5(b), we vacate the sanctions and remand the matter to enable the Commission to reconsider the appropriate penalties.

We have no assurance that the Commission would have imposed the same level of penalties in the absence of its finding of liability for making false statements under Rule 10b-5(b). The Commission expressly grounded its sanctions on its perceptions about the "egregiousness of Lorenzo's conduct" and the "degree of scienter involved," as well as the need to deter others "from engaging in similar misconduct." *Id.* at *12, *14. But the Commission operated under the assumption that Lorenzo devised, and had ultimate authority over, the substance of the false statements contained in the email messages he sent to investors. That assumption, as we have concluded, is unsupported by the record evidence. The Commission in fact specifically based its sanctions in some measure on a belief that Lorenzo improperly sought to "shift blame" by asserting "that he sent the emails at Gregg Lorenzo's direction." *Id.* at *13. But as the record indicates, that is essentially what happened.

Because we "cannot be certain what role, if any," the Commission's misperception that Lorenzo was the "maker" of the false statements ultimately played in its

choice of sanctions, "we must remand" to enable it to reassess the appropriate penalties. *Alliance for Cannabis Therapeutics v. DEA*, 930 F.2d 936, 940-41 (D.C. Cir. 1991). When the Commission does so under a correct understanding about the nature of Lorenzo's misconduct, it can assess "whether the sanction is out of line with the agency's decisions in other cases" involving comparable misconduct—which, as we have observed, is one consideration informing review of penalties for arbitrariness and capriciousness. *Collins v. SEC*, 736 F.3d 521, 526 (D.C. Cir. 2013).

The Commission, in this regard, notes our previous observation that the "Commission is not obligated to make its sanctions uniform, so we will not compare this sanction to those imposed in previous cases." *Geiger v. SEC*, 363 F.3d 481, 488 (D.C. Cir. 2004) (citing *Butz v. Glover Livestock Comm'n Co.*, 411 U.S. 182, 186-87 (1973)). In that vein, we have explained that a mere absence of uniformity will not necessarily render a particular action "unwarranted in law," *id.* at 488, or "unwarranted as a matter of policy," *Kornman*, 592 F.3d at 188. But we have never declined to compare past-and-present Commission sanctions in the context of an arbitrary-and-capricious challenge. In fact, our decision in *Collins* clarified that such a challenge may be brought to review the propriety of the Commission's choice of sanction in a given case as compared with sanctions in comparable situations. *See* 736 F.3d at 526.

* * * * *

For the foregoing reasons, we grant the petition for review in part, vacate the sanctions imposed by the

Commission, and remand the matter for further consideration.

So ordered.

KAVANAUGH, *Circuit Judge*, dissenting: Suppose you work for a securities firm. Your boss drafts an email message and tells you to send the email on his behalf to two clients. You promptly send the emails to the two clients without thinking too much about the contents of the emails. You note in the emails that you are sending the message "at the request" of your boss. It turns out, however, that the message from your boss to the clients is false and defrauds the clients out of a total of $15,000. Your boss is then sanctioned by the Securities and Exchange Commission (as is appropriate) for the improper conduct.

What about you? For sending along those emails at the direct behest of your boss, are you too on the hook for the securities law violation of *willfully* making a false statement or *willfully* engaging in a scheme to defraud?

According to the SEC, the answer is yes. And the SEC concludes that your behavior – in essence forwarding emails after being told to do so by your boss – warrants a *lifetime suspension* from the securities profession, on top of a monetary fine.

That is what happened to Frank Lorenzo in this case. The good news is that the majority opinion vacates the lifetime suspension. The bad news is that the majority opinion – invoking a standard of deference that, as applied here, seems akin to a standard of "hold your nose to avoid the stink" – upholds much of the SEC's decision on liability. I would vacate the SEC's

conclusions as to both sanctions and liability. I therefore respectfully dissent.

* * *

The SEC initiated an enforcement action against Frank Lorenzo and his boss. The boss eventually reached a settlement agreement with the SEC. Apparently thinking he had done little wrong by merely sending emails to two clients at the request of his boss, Lorenzo did not settle.

The case then proceeded through three stages: a trial before an SEC administrative law judge, review by the Commission itself, and then review by this Court. To understand my disagreement with the majority opinion, it is necessary to describe all three acts in this drama.

Act One: The Administrative Law Judge

The case proceeded to trial before an administrative law judge. This was not your usual trial. Surprisingly, the SEC did not present testimony from Lorenzo's boss or from anyone else at the securities firm where Lorenzo worked. Instead, only Lorenzo testified about the extent of his involvement in drafting and sending the emails.

After hearing Lorenzo's testimony and weighing his credibility, the judge concluded that Lorenzo's boss had "drafted" the emails in question and that Lorenzo's boss had "asked" Lorenzo to send the emails to two clients. ALJ Op. at 5 (Dec. 31, 2013), J.A. 906. The judge also concluded that Lorenzo did not read the text of the emails and that Lorenzo "sent the emails without even thinking about the contents." *Id.* at 7, J.A. 908; *see*

id. at 9, J.A. 910 ("Had he taken a minute to read the text . . ."). Furthermore, the judge noted that the emails themselves expressly stated that they were being sent at "the request" of Lorenzo's boss. *Id.* at 5, J.A. 906.

Those factual findings were very favorable to Lorenzo and should have cleared Lorenzo of any serious wrongdoing under the securities laws. At most, the judge's factual findings may have shown some mild negligence on Lorenzo's part. The judge, however, went much further than that. The judge somehow concluded that those findings of fact demonstrated that Lorenzo *willfully* violated the securities laws – meaning that Lorenzo acted with an intent to deceive, manipulate, or defraud. (A finding of willfulness, as opposed to a finding of negligence, matters because it subjects a defendant to much higher penalties.) As a sanction, the judge not only fined Lorenzo, but also imposed a *lifetime suspension* that prevents Lorenzo from ever again working in the securities industry.

The administrative law judge's factual findings and legal conclusions do not square up. If Lorenzo did not draft the emails, did not think about the contents of the emails, and sent the emails only at the behest of his boss, it is impossible to find that Lorenzo acted "willfully." That is Mens Rea 101. Establishing that a defendant acted willfully in this context requires proof at least of the defendant's "intent to deceive, manipulate, or defraud." *Dolphin & Bradbury, Inc. v. SEC*, 512 F.3d 634, 639 (D.C. Cir. 2008) (internal quotation marks omitted). How could Lorenzo have intentionally deceived the clients when he did not draft

the emails, did not think about the contents of the emails, and sent the emails only at his boss's direction?

The administrative law judge's decision in this case contravenes basic due process. A finding that a defendant possessed the requisite mens rea is essential to preserving individual liberty. *See, e.g.*, *Morissette v. United States*, 342 U.S. 246, 250-51, 263 (1952); *see also United States v. Burwell*, 690 F.3d 500, 527 (D.C. Cir. 2012) (en banc) (Kavanaugh, J., dissenting); *United States v. Moore*, 612 F.3d 698, 703 (D.C. Cir. 2010) (Kavanaugh, J., concurring); *Bluman v. FEC*, 800 F. Supp. 2d 281, 292 (D.D.C. 2011) (three-judge panel). As Justice Jackson explained: "The contention that an injury can amount to a crime only when inflicted by intention is no provincial or transient notion. It is as universal and persistent in mature systems of law as belief in freedom of the human will and a consequent ability and duty of the normal individual to choose between good and evil. A relation between some mental element and punishment for a harmful act is almost as instinctive as the child's familiar exculpatory 'But I didn't mean to.'" *Morissette*, 342 U.S. at 250-51 (footnote omitted).

The administrative law judge's opinion in this case did not heed those bedrock mens rea principles. Given the judge's pro-Lorenzo findings of fact, a legal conclusion that Lorenzo "willfully" violated the securities laws makes a hash of the term "willfully," and of the deeply rooted principle that punishment must correspond to blameworthiness based on the defendant's mens rea.

Act Two: The Securities and Exchange Commission

Fast forward to the Securities and Exchange Commission, which heard the appeal of the administrative law judge's decision. Surely the Commission would realize that the administrative law judge's factual findings did not support the judge's legal conclusions and sanctions?

And indeed, the Commission did come to that realization. But instead of vacating the order against Lorenzo, the Commission did something quite different and quite remarkable. In a Houdini-like move, the Commission rewrote the administrative law judge's factual findings to make those factual findings correspond to the legal conclusion that Lorenzo was guilty and deserving of a lifetime suspension.

Recall what the administrative law judge found: that Lorenzo's boss "drafted" the emails, that Lorenzo did not think about the contents of the emails, and that Lorenzo sent the emails only after being asked to do so by his boss. ALJ Op. at 5, J.A. 906. The judge reached those conclusions only after hearing Lorenzo testify and assessing his credibility in person.

Without hearing from Lorenzo or any other witnesses, the Commission simply swept the judge's factual and credibility findings under the rug. The Commission concluded that Lorenzo himself was "responsible" for the emails' contents. *In the Matter of Francis V. Lorenzo*, Securities Act Release No. 9762, Exchange Act Release No. 74836 at 16 (Apr. 29, 2015), J.A. 930. How did the Commission magically explain its decision to discard the administrative law judge's

findings of fact? Easy. In a footnote, the Commission said that it did not need to "blindly" accept the administrative law judge's factual findings and credibility judgments. *Id.* at 16 n.32, J.A. 930 n.32. Voila.

The Commission's handiwork in this case is its own debacle. Faced with inconvenient factual findings that would make it hard to uphold the sanctions against Lorenzo, the Commission – without hearing any testimony – simply manufactured a new assessment of Lorenzo's credibility and rewrote the judge's factual findings. So much for a fair trial.

Act Three: This Court

Fast forward to this Court. To its credit, the majority opinion rightly concludes that Lorenzo did not "make" the statements in the emails for purposes of Rule 10b-5(b) liability. *See Janus Capital Group, Inc. v. First Derivative Traders*, 564 U.S. 135 (2011). And the majority opinion, also to its credit, vacates the grossly excessive lifetime suspension of Lorenzo and sends the case back to the SEC for reconsideration of the appropriate penalties.

So far, so good. But applying what it calls "very deferential" review, the majority opinion upholds the finding of liability against Lorenzo under Section 10(b), Rule 10b-5(a) and (c), and Section 17(a). Maj. Op. 7, 18-25. The majority opinion does so on the ground that Lorenzo willfully engaged in a scheme to defraud even though he did not "make" the statements in the emails.

I disagree on two alternative and independent grounds with the majority opinion's merits analysis.

First, the majority opinion does not heed the administrative law judge's factual conclusions, which were based on the judge's in-person assessment of Lorenzo's testimony at trial. Those factual conclusions demonstrate that Lorenzo lacked the necessary mens rea of willfulness.

To show that Lorenzo willfully engaged in a scheme to defraud, the SEC had to prove that Lorenzo acted with an intent to deceive, manipulate, or defraud. But recall that, as findings of fact, the administrative law judge concluded (after hearing Lorenzo testify) that Lorenzo did not draft the emails, did not think about the contents of the emails, and sent the emails only at the behest of his boss.

In light of the administrative law judge's factual findings, how can Lorenzo be deemed to have willfully engaged in a scheme to defraud? The majority opinion says that the facts found by the administrative law judge are not the right facts. Instead, in reaching its conclusion, the majority opinion relies on the SEC's alternative facts, which the SEC devised on its own without hearing from any witnesses. *See* Maj. Op. 20-21, 26-29 (adopting the SEC's view of the facts over the administrative law judge's view).[1]

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[1] The majority opinion also says that Lorenzo, in his briefing here, does not describe his own state of mind in the way that the administrative law judge did. In other words, the majority opinion says that Lorenzo accepts the SEC's reconstruction of the facts. I disagree. To be sure, Lorenzo advances the alternative argument that he should prevail even if the SEC's reconstruction of the facts is correct. But Lorenzo certainly does not agree with or accept the SEC's reconstruction.

It is true that, under certain circumstances, an agency such as the SEC may re-examine and overturn an administrative law judge's factual findings. *See Universal Camera Corp. v. NLRB*, 340 U.S. 474, 492 (1951). But an agency does not have carte blanche to rewrite an administrative law judge's factual determinations. Rather, an agency must act reasonably when it disregards an administrative law judge's factual findings, a point the SEC's attorney expressly acknowledged at oral argument. *See* Tr. of Oral Arg. at 28. It is black-letter law, therefore, that "a contrary initial decision" by an administrative law judge "may undermine the support for the agency's ultimate determination." Ronald M. Levin & Jeffrey S. Lubbers, *Administrative Law and Process* 101 (6th ed. 2017). And here is the key principle that speaks directly to this case: "When the case turns on eyewitness testimony . . . the initial decision should be given considerable weight: the ALJ was able to observe the demeanor of the witnesses and assess their credibility and veracity first hand." *Id.*

Moreover, in making this point, the majority opinion draws a dichotomy between Lorenzo's good-faith belief (as noted in his briefs) in the accuracy of the emails and Lorenzo's statement that he did not think about the contents of the email. That is a false dichotomy. When forwarding an email on behalf of your boss, you could have a good-faith belief in its accuracy because you trust your boss, or at least have no reason to delve deeply into the particulars of the email's contents, not because you have necessarily read or independently verified the contents of the email. The majority opinion notes that Lorenzo, "as of November 2009," did not trust his boss. Maj. Op. 27. But that date is of course *after* the events at issue in this case.

In my view, the majority opinion misapplies those black-letter principles. Contrary to the majority opinion's acceptance of the SEC's reconstruction of the facts in this case, I would conclude that the SEC's rewriting of the administrative law judge's findings of fact was utterly unreasonable and should not be sustained or countenanced by this Court. Given that Lorenzo was the only relevant witness at trial (dwell again on that point for a few moments) and given that his credibility was central to the case, the SEC had no reasonable basis to run roughshod over the administrative law judge's findings of fact and credibility assessments. In short, the SEC's rewriting of the findings of fact deserves judicial repudiation, not judicial deference or respect.

Instead of deferring to the SEC's creation of an alternative factual record, as the majority opinion does, we should examine the administrative law judge's underlying findings of fact and ask whether *those findings* suffice to support the conclusion that Lorenzo willfully engaged in a scheme to defraud. The answer to that question, as explained above, is a clear no.[2]

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[2] At oral argument, counsel for the SEC actually stated that it would have been "more difficult" for the SEC to find Lorenzo liable if Lorenzo's email had said that it was being sent "on behalf of" his boss instead of "at the request of" his boss. Counsel for the SEC asserted that those two phrases were "meaningfully different." Tr. of Oral Arg. at 30. With respect, I find that argument absurd and an illustration of how the Commission jumped the rails in this case. It is startling that the SEC thinks such a wafer-thin semantic distinction can make the difference between (i) a lifetime suspension from your chosen profession and (ii) no penalty at all.

Second, put that aside. Even if I am wrong about the first point, the majority opinion still suffers from a separate flaw, in my view.

The majority opinion creates a circuit split by holding that mere misstatements, standing alone, may constitute the basis for so-called scheme liability under the securities laws – that is, willful participation in a scheme to defraud – even if the defendant did not make the misstatements.[3] No other court of appeals has adopted the approach that the majority opinion adopts here. Other courts have instead concluded that scheme liability must be based on conduct that goes beyond a defendant's role in preparing mere misstatements or omissions made by others. *See, e.g.*, *Public Pension Fund Group v. KV Pharmaceutical Co.*, 679 F.3d 972, 987 (8th Cir. 2012); *WPP Luxembourg Gamma Three Sarl v. Spot Runner, Inc.*, 655 F.3d 1039, 1057 (9th Cir. 2011); *Lentell v. Merrill Lynch & Co.*, 396 F.3d 161, 177 (2d Cir. 2005); *see also SEC v. Kelly*, 817 F. Supp. 2d 340, 343-44 (S.D.N.Y. 2011). Otherwise, the SEC would be able to evade the important statutory distinction between primary liability and secondary (aiding and abetting) liability. After all, if those who aid and abet a misstatement are themselves primary violators for engaging in a scheme to defraud, what would be the point of the distinction between primary and secondary liability?

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[3] On page 31, the majority opinion ultimately appears to acknowledge the circuit split: "Insofar as those courts of appeals would find Lorenzo's actions to lie beyond the reach of those provisions, we read the provisions differently."

The distinction between primary and secondary liability matters, particularly for private securities lawsuits. For decades, however, the SEC has tried to erase that distinction so as to expand the scope of primary liability under the securities laws. For decades, the Supreme Court has pushed back hard against the SEC's attempts to unilaterally rewrite the law. *See Janus*, 564 U.S. 135; *Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc.* 552 U.S. 148 (2008); *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164 (1994). Still undeterred in the wake of that body of Supreme Court precedent, the SEC has continued to push the envelope and has tried to circumvent those Supreme Court decisions. *See, e.g., In the Matter of John P. Flannery & James D. Hopkins*, Release No. 3981 (Dec. 15, 2014). This case is merely the latest example.[4]

I agree with the other courts that have rejected the SEC's persistent efforts to end-run the Supreme Court.

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[4] In this case, the SEC relied on its prior decision in *Flannery*. But as one respected commentator persuasively explained, the SEC's *Flannery* decision is wrong. "The substantive concern is that the Commission defined primary liability under portions of the major anti-fraud provisions in expansive ways that disregarded the reasoning and rationale of the Supreme Court and some courts of appeals. The Supreme Court has sought to clarify the distinction between primary and secondary liability under Rule 10b-5, yet the Commission's *Flannery* decision all but eradicated the distinction and committed the same error with Section 17(a). It sought to regain the ground on primary liability that was lost in *Stoneridge* and *Janus* and then went further with novel constructions of primary liability based on lawful, non-deceptive actions or exorbitant doctrines of but-for causality." Andrew N. Vollmer, *SEC Revanchism and the Expansion of Primary Liability Under Section 17(a) and Rule 10b-5*, 10 VA. L. & BUS. REV. 273, 340 (2016).

I therefore respectfully disagree with the majority opinion that Lorenzo's role in forwarding the alleged misstatements made by Lorenzo's boss can be the basis for scheme liability against Lorenzo.

Taking a step back on the scheme liability point, moreover, think about the oddity of the majority opinion's combined legal rulings today. The majority opinion emphatically holds that Lorenzo did not "make" the statements in the emails. In reaching that conclusion, the majority opinion accurately says that "Lorenzo transmitted statements devised by" Lorenzo's boss at his boss's "direction." Maj. Op. 16. The majority opinion also correctly notes that Lorenzo's boss "asked Lorenzo to send the emails, supplied the central content, and approved the messages for distribution." Maj. Op. 17. At the same time, however, the majority opinion emphatically holds that Lorenzo nonetheless willfully engaged in a scheme to defraud solely because of the statements made by his boss. That combined holding makes little sense (at least to me) under the facts of this particular case. Nor does it make much sense under the law, which is presumably why the other courts of appeals have rejected that kind of legal jujitsu. In these circumstances, perhaps the alleged offender (here, Lorenzo) could have been charged with aiding and abetting, if the relevant mens rea requirements for aiding and abetting liability were met. But Lorenzo may not be held liable as a primary violator, in my view.

* * *

Administrative adjudication of individual disputes is usually accompanied by deferential review from the Article III Judiciary. That agency-centric process is in

some tension with Article III of the Constitution, the Due Process Clause of the Fifth Amendment, and the Seventh Amendment right to a jury trial in civil cases. *See generally* PHILIP HAMBURGER, IS ADMINISTRATIVE LAW UNLAWFUL? 227-57 (2014). That tension is exacerbated when, as here, the agency's political appointees – without hearing from any witnesses – disregard an administrative law judge's factual findings. That said, the Supreme Court has allowed administrative adjudication ever since *Crowell v. Benson*, 285 U.S. 22 (1932). But the premise of *Crowell v. Benson* is that, putting aside any formal constitutional problems with the notion of administrative adjudication, the administrative adjudication process will at least operate with efficiency and with fairness to the parties involved. This case, among others, casts substantial doubt on that premise.

Securities brokers such as Frank Lorenzo obviously do not tug at the judicial heartstrings. And maybe Lorenzo really is guilty of negligence (or worse). But before the SEC reaches such a conclusion, Lorenzo is entitled to a fair process just like everyone else. *Cf. United States v. Burwell*, 690 F.3d 500, 527 (D.C. Cir. 2012) (en banc) (Kavanaugh, J., dissenting). He has not received a fair process in this case.

I hope that the SEC on remand pays attention, comes to its senses, and (at a minimum) dramatically scales back the sanctions in this case. Indeed, notwithstanding the majority opinion, I hope that the SEC, on its own motion, goes further than that: The SEC should vacate the order against Lorenzo in its entirety and either end this case altogether or (if

appropriate and permissible) fairly start the process anew before the administrative law judge.

I firmly disagree with the majority opinion's decision to sustain the SEC's findings of liability under Section 10(b), Rule 10b-5(a) and (c), and Section 17(a). I respectfully dissent.

APPENDIX B

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 9762 / April 29, 2015

SECURITIES EXCHANGE ACT OF 1934
Release No. 74836 / April 29, 2015

Admin. Proc. File No. 3-15211

[Filed April 29, 2015]

In the Matter of	)
	)
FRANCIS V. LORENZO	)
c/o Robert G. Heim	)
Meyers & Heim LLP	)
444 Madison Ave., 30th Floor	)
New York, NY 10022	)
	)

OPINION OF THE COMMISSION

CEASE-AND-DESIST PROCEEDING

Grounds for Remedial Action

Antifraud Violations

A formerly registered representative committed securities fraud by sending two potential investors emails that he knew contained false and misleading

information about his firm's client. *Held*, it is in the public interest to bar respondent from associating with an investment adviser, broker, dealer, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization and from participating in an offering of penny stock; order him to cease and desist from committing or causing any violations or future violations of the provisions violated; and order him to pay a civil monetary penalty of $15,000.

APPEARANCES:

Robert G. Heim, for Francis V. Lorenzo.

Alex Janghorbani and *Jack Kaufman*, for the Division of Enforcement.

Appeal filed: January 27, 2014
Last brief received: May 7, 2014
Oral argument: March 30, 3015

I.

Francis V. Lorenzo, formerly a registered representative, appeals an administrative law judge's finding that he violated Section 17(a) of the Securities Act of 1933, Section 10(b) of the Securities Exchange Act of 1934, and Exchange Act Rule 10b-5 by sending false and misleading statements to prospective investors.[1] For these violations, the law judge barred Lorenzo from the securities industry, ordered him to cease and desist from violating the antifraud

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[1] *Francis V. Lorenzo*, Initial Decision Release No. 544, 2013 WL 6858820 (Dec. 31, 2013).

provisions, and ordered him to pay a third-tier civil monetary penalty of $15,000. The Division cross-appeals the imposition of the civil penalty and asks that we increase the penalty to "at least $100,000."

The charges against Lorenzo stem from emails he sent to retail customers that contained false and misleading statements about a debenture offering by his client, Waste2Energy Holdings, Inc. ("W2E"). The emails promised the customers that their investment would have three "layers of protection": (i) that W2E had more than $10 million "in confirmed assets"; (ii) that W2E had "purchase orders and [letters of intent] for over $43 mm in orders"; and (iii) that Lorenzo's employer, Charles Vista, LLC, had "agreed to raise additional monies to repay these Debenture holders (if necessary)." Lorenzo admitted at the hearing that he knew each of these statements was false and/or misleading when he sent them. For the reasons below, his conduct violated the antifraud provisions of the federal securities laws and warrants imposition of an industry-wide bar, a cease-and-desist order, and a $15,000 civil penalty. Our findings are based on an independent review of the record.[2]

II.

Lorenzo was director of investment banking at Charles Vista, LLC, a registered broker-dealer owned

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[2] We note that Rule of Practice 451(d), 17 C.F.R. § 201.451(d), permits a member of the Commission who was not present at oral argument to participate in the decision of the proceeding if that member has reviewed the oral argument transcript before such participation. Commissioner Aguilar has made the requisite review.

by Gregg Lorenzo,[3] from February 2009 through February 2010 (the relevant time here). As Lorenzo described it, Charles Vista was "a small boiler room." Its registered representatives, Lorenzo explained, engaged in high-pressure sales tactics, were "not being a hundred percent accurate in their presentations" to brokerage clients, and seemed to be "stretching the truth."[4] Lorenzo's only investment banking client during the relevant time was W2E. Lorenzo's responsibilities included preparing offering documents for W2E; making sure the company made all material disclosures; and conducting due diligence, including reviewing the company's financial statements and public filings.

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[3] Gregg Lorenzo is not related to the respondent. We will refer to the respondent as "Lorenzo" and to Gregg Lorenzo as "Gregg Lorenzo."

[4] Charles Vista and Gregg Lorenzo settled related charges against them in November 2013. *Gregg C. Lorenzo*, Securities Act Release No. 9480, 2013 WL 6087352 (Nov. 20, 2013) (Settlement Order). Before that settlement, on June 17, 2013, Charles Vista had already withdrawn its registration as a broker-dealer, and FINRA cancelled Charles Vista's membership on July 31, 2013, for failure to pay outstanding fees. We take official notice of this information on BrokerCheck, an electronic database maintained by FINRA and available at http://brokercheck.finra.org. *See* 17 C.F.R. § 201.323 (rule of practice relating to official notice). On June 18, 2013, FINRA also permanently barred Gregg Lorenzo from association with any member for his refusal to comply with multiple requests to appear for an on-the-record interview. *See* http://brokercheck.finra.org (last visited April 28, 2015).

A. Lorenzo knew that W2E was in dire financial condition.

According to W2E's Form 8-K (filed June 3, 2009), the company developed technology for customers "to convert[] biomass or other solid waste streams traditionally destined for landfill or incineration into clean renewable energy." But according to Lorenzo, W2E's technology "didn't really work" and the company's "financial well-being was horrible." As the company explained in its Form 8-K, W2E had been "operating at a substantial operating loss each year since [its] inception," had "a substantial accumulated deficit," and expected "to continue to incur substantial losses for the foreseeable future." The company's unaudited financial statements, which were included in the Form 8-K, disclosed that the company had total assets (as of December 31, 2008) of approximately $14 million and total liabilities of approximately $9.5 million. Of its approximately $14 million in total assets, W2E attributed more than $10 million to "intangibles," which consisted of intellectual property. The company's Form 8-K further disclosed that W2E's business operations depended on generating substantial revenues from one customer, Ascot Environmental Ltd., which subjected W2E to "significant financial and other risks in the operation of [its] business." The company also disclosed that its independent registered auditors had "expressed substantial doubt about [its] ability to continue as a going concern."

Lorenzo testified that he saw the company's Form 8-K shortly after the company issued it and was concerned at the time that W2E's purported intangible

assets were not actually worth $10 million. He instead believed that the intangibles were a "dead asset." There was "no way," Lorenzo testified, that the company could "get even close to $10 million" for the assets, and the company would be "lucky" to receive $1 million for the assets. Lorenzo also thought it was significant that W2E's financial statements were unaudited because "there is way too much risk for investors" without an audit.

B. Lorenzo helped prepare the private placement memorandum for W2E's convertible debentures offering.

By mid-August 2009, W2E was finalizing an audit of its financial statements for the fiscal year ending March 31, 2009, so that those statements could be included in its Form 10-Q. Around the same time, the company also began preparing a private placement of up to $15,000,000 in 12 percent convertible debentures.[5] Charles Vista was the exclusive placement agent for the debenture offering, for which the firm was to be paid nearly 20 percent of the offering proceeds—an amount Lorenzo described as "exorbitant." Lorenzo testified that he was promised seven to nine percent of any money he raised from the offering, but that he ultimately received only one percent of the money he raised.

Lorenzo helped W2E prepare the private placement memorandum ("PPM"). At least twice during that

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[5] Debentures are "debt secured only by the debtor's earning power, not by a lien on any specific asset." BLACK'S LAW DICTIONARY 330 (9th ed. 2009), *available at* Westlaw Blacks.

process, Lorenzo asked W2E to disclose the $10 million of intangible assets in its PPM because he thought it was "material." On August 26, 2009, Lorenzo emailed edits and comments regarding the PPM to the company, writing that, "[w]e want to mention that the company has IP and Intangibles valued at $10,038,558" (emphasis in original). Lorenzo testified that he based that number on the unaudited financial statements in W2E's Form 8-K. On September 1, 2009, Lorenzo emailed additional edits to W2E, again asking that they include a reference to the company's intangible assets. But this time Lorenzo left the value of the assets blank because, he testified, he was no longer sure what the assets were worth. Lorenzo also admitted that, as early as April 2009, he began repeatedly telling Gregg Lorenzo not to sell W2E's debentures as being collateralized by the $10 million asset. Lorenzo explained that he did so because he knew that the assets "provided no protection" to investors and that, if the company defaulted on the debentures, investors would not be able to recoup their money through the liquidation of those assets.

Lorenzo did not recall that anyone from W2E ever responded to his requests to disclose the intangible assets, and ultimately W2E did not disclose a dollar value for its intangible assets in its final PPM, which was dated September 9, 2009. Instead, W2E disclosed only that it had "a significant IP portfolio." The company also reiterated many of the disclosures from its earlier Form 8-K, including that the company "had significant operating losses," did "not expect to be profitable for at least the foreseeable future," and could not "predict when we might become profitable, if ever." The company further stated in the PPM that it was

"wholly reliant on the net proceeds from this Offering to fund [its] proposed business" and that, "[i]f less than the Maximum Offering [$15 million] is sold, [it] will have an immediate need for substantial additional capital and may only have enough capital for less than one month of proposed operations." The company added: "If we are unable to raise substantial capital, investors will lose their entire investment." Lorenzo testified that he received and reviewed the final PPM.

C. W2E announced a complete write down of its intangible assets.

On October 1, 2009, approximately one month after finalizing the PPM, W2E filed an amended Form 8-K and Form 10-Q. Those filings contained audited financial statements for the fiscal year ended March 31, 2009, and reported a complete write-off of W2E's $10 million intellectual property asset and $496,594 in good will. The company stated that, as of March 31, 2009, its total assets were only $370,552 and that its sole contract (with Ascot Environmental) was causing it to incur a net loss.

Lorenzo testified that, although it was his responsibility to review W2E's filings, he only "skimmed the filings and [he] missed the write off." Lorenzo nevertheless acknowledged that, on October 5, four days after the company filed its financial statements disclosing the write down, W2E's CFO sent Lorenzo an email, stating: "The accumulated deficit we have reported is due to three primary issues [including] . . . . [w]rite off of all of our intangible assets . . . of about $11 million." (emphasis in original). Lorenzo admitted that he reviewed the email and therefore understood, by at least October 5, 2005, that the

company had written off the $10 million in intangible assets.

D. Lorenzo emailed two prospective investors about W2E's debenture offering, falsely assuring them of three "layers of protection."

On October 14, 2009, Lorenzo sent a one-page email to two retail customers—Vishal Goolcharan and William Rothe—entitled "W2E Debenture Deal Points." The emails stated that, "[a]t the request of Adam Spero and Gregg Lorenzo, the Investment Banking division of Charles Vista has summarized several key points of the Waste2Energy Holdings, Inc. Debenture Offering."[6] The emails then told the investors, in bold type, "Please read the Offering Memorandum, including all the 'Risk Factors,'" but Lorenzo acknowledged that he did not know whether either customer ever actually saw the PPM because he never sent them one.

Lorenzo's emails next summarized the offering's basics, including the debenture's term and the interest rate, and promised that investors would be paid first in the event of liquidation. The emails then assured investors:

> There are 3 layers of protection:
>
> (I) The Company has over $10 mm in confirmed assets

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[6] This quote is from the email to Goolcharan. The email to Rothe did not mention Adam Spero, stating only that Gregg Lorenzo had asked the investment banking division to summarize the debenture offering.

(II) The Company has purchase orders and LOI's [sic] for over $43 mm in orders

(III) Charles Vista has agreed to raise additional monies to repay these Debenture holders (if necessary).

After noting the debenture holders' right to convert their debt into common stock and to receive a warrant to purchase shares, the emails concluded, "Please call with any questions—Truly, Francis V. Lorenzo."

Lorenzo admitted that, at the time he sent the emails, he knew that the statements about all three layers of supposed protection were false, misleading, or both. Lorenzo acknowledged, for example, that the statement about the company having $10 million in confirmed assets "was never true." Lorenzo testified that he took the $10 million number from the company's unaudited financial statements in its June 2009 Form 8-K, which stated that the company had $10 million in intangible assets. Yet Lorenzo admitted that this number had never been confirmed by auditors or the company; that he knew by the time he sent the emails that the company had written off those assets; and that he himself did not believe the company's intangible assets had been worth anywhere close to $10 million. Lorenzo also admitted that, before sending the emails, he knew that the $43 million in purported purchase orders and LOIs were based only on a single, non-binding, letter of intent, which did not obligate the potential purchaser (or W2E) to do anything. He further acknowledged that, by sometime in September, he had "lost confidence that this 43 million was ever going to happen." Lorenzo similarly admitted that he

knew, at the time he sent the emails, that Charles Vista had not agreed to raise any additional money to repay debenture investors.

Lorenzo explained his sending the emails as a "mistake." Lorenzo testified that he sent the emails without thinking about the contents: "I don't want to minimize the severity of it but, you know, I just didn't give it much thought at the time. My boss asked me to send these e-mails out and I sent them out." On December 18, 2009, one of the email recipients, Vishal Goolcharan, invested $15,000 in W2E's debenture offering (jointly with Roslyn Parmasad). Lorenzo earned one percent (or $150) from that investment.

E. Lorenzo provided misleading investigative testimony about Gregg Lorenzo, Charles Vista, and W2E's debenture offering.

The Division subsequently launched an investigation into Lorenzo and his employer, Charles Vista and Gregg Lorenzo, during which Lorenzo testified under oath in November 2009. Lorenzo told Commission staff that Gregg Lorenzo was an "honest guy"; that he was proud of what Gregg Lorenzo planned at Charles Vista; and that he and Gregg Lorenzo were working toward their "vision" of building Charles Vista into a "high quality investment banking [d]ivision." Lorenzo further testified that he "believed in" selling W2E's debentures and described the sale as one of several "high quality projects."

Lorenzo's subsequent hearing testimony was far different. As noted above, for instance, Lorenzo described Charles Vista as a boiler room and expressed concern that the firm's registered representatives were

not entirely truthful when selling securities. Lorenzo also testified that, by November 2009, "there [was] no way on God's green earth [he] thought Gregg Lorenzo was an honest guy"; that, by October 2009, it was "a stretch" to say that he was proud of the work he and Gregg Lorenzo were doing at Charles Vista; and that he did not think that Charles Vista was a high-quality investment bank. Nor did Lorenzo describe W2E's debenture offering as a high-quality project, instead labeling it a "toxic convertible debt spiral."

Lorenzo testified that he began looking for a new job sometime in October or November 2009 because he had become "unhappy" at Charles Vista. He eventually left Charles Vista in February 2010 and became a managing director at Hunter Wise Securities, LLC, a broker-dealer where Lorenzo focused primarily on arranging funding for both public and private companies. Lorenzo represents that he resigned from this position on April 15, 2014. He is not currently registered.[7]

III.

The Division alleges that Lorenzo violated Exchange Act Section 10(b), Exchange Act Rule 10b-5, and Securities Act Section 17(a) by sending two materially misleading emails to customers. Section 10(b) makes it "unlawful for any person directly or indirectly . . . to use or employ, in connection with the purchase or sale of any security . . . any manipulative or deceptive device or contrivance in contravention of"

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[7] *See* http://brokercheck.finra.org (last visited April 28, 2015).

Commission rules.[8] Rule 10b-5 implements the Commission's authority under Section 10(b).[9] It does so through three subsections that are "mutually supporting rather than mutually exclusive."[10] The first, Rule 10b-5(a), prohibits "directly or indirectly . . . employ[ing] any device, scheme, or artifice to defraud."[11] The second, Rule 10b-5(b), prohibits "directly or indirectly . . . mak[ing] any untrue statement of a material fact or [omitting] to state a material fact necessary in order to make the statements made . . . not misleading."[12] The third, Rule 10b-5(c), prohibits "directly or indirectly . . . engag[ing] in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person."[13]

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[8] 15 U.S.C. § 78j(b).

[9] *See John P. Flannery*, Securities Exchange Act Release No. 73840, 2014 WL 7145625, at *10 (Dec. 15, 2014) (citing *United States v. Zandford*, 535 U.S. 813, 816 n.1 (2002)), *appeal docketed*, No. 15-1080 (1st Cir. Jan. 16, 2015).

[10] *Id.* (citing *Cady, Roberts & Co.*, Exchange Act Release No. 6668, 40 SEC 907, 1961 WL 60638, at *4 (Nov. 8, 1961)).

[11] 17 C.F.R. § 240.10b-5(a).

[12] *Id.* § 240.10b-5(b).

[13] *Id.* § 240.10b-5(c).

Section 17(a), in turn, makes it unlawful to engage in certain conduct in "the offer or sale of securities."[14] Like Rule 10b-5, Section 17(a) expresses its prohibitions in three "mutually supporting" subsections.[15] Relevant here is Section 17(a)(1), which, like Rule 10b-5(a), prohibits "directly or indirectly . . . employ[ing] any device, scheme, or artifice to defraud."[16] Liability under Section 17(a) and Rule 10b-5 requires a showing of scienter, which is "a mental state embracing intent to deceive, manipulate, or defraud."[17] As explained below, we agree with the Division that Lorenzo violated these provisions by knowingly sending materially misleading emails to prospective investors.

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[14] 15 U.S.C. § 77q(a). We find, and there is no dispute, that all of the statements and omissions at issue here were made in connection with the offer or sale of securities.

[15] *Cady, Roberts & Co.*, 1961 WL 60638, at *4.

[16] 15 U.S.C. § 77q(a)(1).

[17] *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 n.12 (1976). Scienter may be established through "a heightened showing of recklessness." *Flannery*, 2014 WL 7145625, at *10 n.24. This has been "defined as . . . an extreme departure from the standards of ordinary care, and which presents a danger of misleading buyers or sellers that is either known to the [actor] or is so obvious that the actor must have been aware of it." *David Henry Disraeli*, Exchange Act Release No. 57027, 2007 WL 4481515, at *5 (Dec. 21, 2007); *accord SEC v. Ficken*, 546 F.3d 45, 47–48 (1st Cir. 2008) (finding that Section 17(a)(1), Section 10(b), and Rule 10b–5 require only "a high degree of recklessness" (quotations omitted)); *Rockies Fund, Inc. v. SEC*, 428 F.3d 1088, 1093 (D.C. Cir. 2005) (finding that Rule 10b-5 requires a showing of extreme recklessness).

A. The emails that Lorenzo sent were misleading.

We first examine whether the emails Lorenzo sent were misleading. There is no dispute that the statement regarding the first layer of protection—that the company had "over $10 mm in confirmed assets"—was misleading. In fact, Lorenzo admitted that this statement had never been true. Lorenzo derived that number from the $10 million in intangible assets listed in the company's unaudited financial statements. But by the time Lorenzo wrote the emails, W2E had written off those assets and disclosed that it had only $400,000 in assets remaining. And Lorenzo himself testified that he did not believe at the time he sent the emails that the company's intangible assets were worth anywhere close to $10 million. Lorenzo's emails to customers stating otherwise were therefore plainly false and would mislead any reader about the state of the company's assets.

The statement regarding the second layer of supposed protection—that the company had "purchase orders and LOI's for over $43 mm in orders"—was also misleading. As Lorenzo testified, this assurance was based on a single, non-binding, letter of intent, which did not obligate the potential purchaser (or W2E) to do anything. Lorenzo argues on appeal that W2E's CEO "believed in the validity of this LOI [and] that it would turn into customer orders." But that assertion is based on Lorenzo's own, self-serving testimony about what W2E's CEO may have believed. And even if that *is* what the CEO believed, it is still only vague speculation that the LOI *could* "turn into customer orders." Lorenzo's written statements promising the prospective investors that the company *had* over $43

million in orders was therefore false and would mislead any reader about the company's future revenue.

The third statement—that Charles Vista had agreed to raise additional money—was also misleading. As Lorenzo admitted, Charles Vista had no such agreement with W2E. Lorenzo nevertheless argues on appeal that the emails' assurance to the contrary was "not an unreasonable statement because Gregg Lorenzo had on a number of prior occasions raised money to pay back debenture holders" and because Gregg Lorenzo had been meeting with other broker-dealers about raising additional funds for W2E. But even if these claims were true, they establish only the theoretical possibility that Charles Vista could have raised additional money to repay investors, not that it had agreed to do so (as Lorenzo's emails claimed). Lorenzo also admitted that, even if Charles Vista *had* agreed to raise additional money, it would have had a difficult time doing so: Charles Vista, Lorenzo explained, did not have "the buying power or resources to properly fund Waste2Energy in order to repay the debentures." Lorenzo's assurance that Charles Vista had agreed to raise additional money was therefore false and would mislead any investor about the prospects of Charles Vista actually raising additional money in the event of W2E's default.

B. The misrepresentations in the emails were material.

We next examine whether the misrepresentations were material. For a misstatement to be material, "there must be a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly

altered the 'total mix' of information made available."[18] It does not matter whether "disclosure of the omitted fact would have caused the reasonable investor to change" his behavior.[19]

That standard is met here. Lorenzo's emails concerned an unsecured debt offering by a company in dire financial straits. Yet instead of mentioning any of the substantial risks involved, Lorenzo falsely assured retail customers that their investment would be protected in three different ways.[20] A reasonable

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[18] *Basic Inc. v. Levinson*, 485 U.S. 224, 231–32 (1988) (quoting *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976)).

[19] *TSC Indus.*, 426 U.S. at 449.

[20] We note that, while the emails directed the customers to read the PPM (which disclosed some of the risks involved with the offering but not the company's $10 million write-down), Lorenzo never sent them the disclosure document and did not know whether they ever saw it. *Cf. New Jersey Carpenters Health Fund v. Royal Bank of Scotland*, 709 F.3d 109, 127 (2d Cir. 2013) (explaining that "'[t]here are serious limitations on a corporation's ability to charge its stockholders with knowledge of information omitted from a document such as a . . . prospectus on the basis that the information is public knowledge and otherwise available to them'"); *SEC v. Morgan Keegan & Co., Inc.*, 678 F.3d 1233, 1252 (11th Cir. 2012) (rejecting defendant's motion for summary judgment on the "materiality" issue by noting that the "misstatements must be considered in the factual context of a weak, or non-existent, distribution of the written disclosures"). And while W2E previously disclosed the $10 million write-down and lack of other assets in its Forms 8-K and 10-Q, that information was more than six months old when Lorenzo sent the emails. A reasonable investor could therefore believe, as Lorenzo's emails implied, that the company's fortunes had changed in that time—a misimpression furthered by Lorenzo's other false claims

investor would have found the accuracy of any one of these promises of protection to significantly alter "the 'total mix' of information made available" given the company's precarious financial state and the offering's unsecured nature.[21] That all three statements were inaccurate—meaning that any investment had essentially no protection—made the misrepresentations all the more material to prospective investors.

C. Lorenzo acted with scienter when sending the materially misleading emails to customers.

We next turn to the question of scienter—namely, whether Lorenzo knew or must have known that his emails were materially misleading.[22] That standard is met here. Regarding the first layer of supposed protection (that the company had "over $10 mm in confirmed assets"), Lorenzo admitted knowing that W2E had written off its $10 million in intangible assets when he sent the emails. Lorenzo also acknowledged that, even before the write-off, he had considered the supposed $10 million in intangibles to be "dead assets" because there was "no way" that W2E could "get even close to $10 million" for them. Lorenzo further admitted that, for more than half a year before sending the emails, he repeatedly told Gregg Lorenzo not to sell the debentures as being collateralized by the intangible

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about the company's supposedly strong revenue stream of $43 million in purchase orders and letters of intent and Charles Vista's supposed willingness to raise additional funds.

[21] *TSC Indus.*, 426 U.S. at 449.

[22] *See supra* note 17 (defining scienter).

assets because he understood that those assets would not protect the customers' investment.

Lorenzo's testimony similarly establishes that he knew or must have known that the statement regarding the second layer of supposed protection (the alleged $43 million in purchase orders and LOIs) was both false and misleading. Lorenzo admitted that, before sending the emails, he knew that the $43 million in purported purchase orders and LOIs were based on only a single, non-binding letter of intent, which did not obligate the potential purchaser (or W2E) to do anything and that, by sometime in September, Lorenzo had "lost confidence that this 43 million was ever going to happen." He even acknowledged that, while he could not say with "a hundred percent" certainty that the statement was misleading, "I could see it being misleading."

And regarding Lorenzo's third misstatement (Charles Vista's supposed agreement to raise additional money), Lorenzo admitted that, at the time of the emails, he knew that Charles Vista had not agreed to raise any additional money to repay debenture investors. He further acknowledged that, even if such an agreement had existed, he knew, "long before October," that W2E would have had a difficult time raising additional money because Charles Vista had already invested 70 percent of all of its brokerage clients' money in W2E, an amount Lorenzo acknowledged was "way too much." Because of this, Lorenzo admitted, "Charles Vista would not have the buying power or resources to properly fund Waste2Energy in order to repay the debentures." In fact, when asked at the hearing whether his assurance

that Charles Vista would raise additional money was misleading, he admitted that "you couldn't hang your hat on it."

Despite this evidence of scienter, Lorenzo asserts on appeal that he had a good faith belief in the truthfulness of his emails and that there is no basis for concluding that he "acted with intent to deceive investors." He claims it was "entirely reasonable" to state that the company had $10 million in confirmed assets because that figure was taken from the company's unaudited financial statements, which had been filed with the Commission. Lorenzo further reasons that it was not reckless for him to have missed the company's subsequent write off because W2E allegedly "buried" that fact in its filings and failed to fulfil a contractual agreement that Lorenzo claimed the company had with Charles Vista to immediately disclose any material changes in W2E's financial condition. The write down "needed to be emphasized," Lorenzo testified, "not minimized and not hidden in a regulatory document. There [are] no disclosures anywhere, anywhere that this asset may have been written off to 95 percent. None. Zero."

These contentions are both implausible and contradicted by Lorenzo's testimony. W2E was Lorenzo's only investment banking client, and it was his job to review the company's financial statements. Lorenzo knew at the time he received the filings that W2E was in dire financial condition. He had also believed for months that the company's assets were not worth "even close to $10 million." That Lorenzo could have looked at the company's filings, which was his job, and missed what was one of the most pertinent facts in

them—the valuation of the company's assets—is either untrue or extreme recklessness.[23] But even if Lorenzo did initially miss W2E's write-down, Lorenzo admitted that he learned about it a few days later, when the company's CFO emailed him about it. In fact, when asked during his investigative testimony about whether he knew at the time he sent the emails that the statements about the three layers of protection were inaccurate and misleading, he answered, "I can't sit here and say that I didn't know."

Lorenzo also admitted during the hearing that he did not believe that W2E was a worthwhile investment; that he had "lost confidence in the management of Waste2Energy to grow the business"; and that he thought it was "highly unlikely . . . that [W2E] was going to have enough corporate growth in order to pay back the money that it had borrowed." These worries about the company's offering, combined with his long-standing concern about the legitimacy of the company's $10 million in claimed assets, establish that it was at least extremely reckless for Lorenzo to email customers

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[23] Lorenzo points to Charles Vista's chief compliance officer's sending an email to Charles Vista's brokers (which contained a research report showing that W2E's assets exceeded $10 million) as evidence that the compliance officer also missed the asset write down in W2E's financial statements and thus represented "some evidence that Mr. Lorenzo was not acting recklessly or negligently when he missed it." But there was no testimony or other evidence introduced about the circumstances surrounding the distribution of that document, and the mere fact that, for whatever unknown reason, a compliance officer sent an inaccurate research report internally to the firm's brokers is neither analogous to, nor an excuse for, Lorenzo's knowingly sending materially misleading emails to prospective investors.

that their investment would be protected by $10 million in confirmed assets without first checking that statement against the company's most recent financial statements.[24]

We also disagree with Lorenzo's claim that his forwarding the company's public filings (which contained the $10 million write down) to Charles Vista's brokers shortly after receiving them shows that he lacked the intent to misrepresent or hide W2E's financial condition. Forwarding the company's filings internally to Charles Vista employees does not explain or excuse Lorenzo's subsequent decision to send materially misleading emails externally to firm customers. And the record contains evidence of at least one possible motive for misleading potential investors: Lorenzo knew when he sent the emails that his employer, Charles Vista, would earn what he described as an "exorbitant" fee from any successful sales and that he would receive a portion of those fees.[25] Lorenzo's testimony clearly establishes that he either

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[24] *Cf. Rita J. McConville*, Exchange Act Release No. 51950, 2005 WL 1560276, at *9 n.36 (June 30, 2005) (finding violations of Section 10(b) and Rule 10b-5 because "it was at least reckless [for respondent to] not actually review the [Form 10-K] about which she was making representations"), *pet. for review denied*, 465 F.3d 780 (7th Cir. 2006).

[25] *Cf. Donald L. Koch*, Exchange Act Release No. 72179, 2014 WL 1998524, at *14 (May 16, 2014) ("[P]roof of motive is not required where there is direct evidence of manipulative intent; it is only where direct evidence of scienter is lacking that circumstantial evidence of intent, such as motive, becomes critical.").

knew or must have known that his emails would materially mislead investors.[26]

Nor are we persuaded by Lorenzo's assertion that his sending the emails was simply a "mistake." Lorenzo was well aware that the emails falsely represented crucial facts about W2E and its debenture offering. Sending emails to customers was also not a normal occurrence for Lorenzo. In fact, he contends that these emails were the only time he ever communicated with customers. His claim that he nevertheless "didn't give [sending the emails] much thought" is therefore implausible. And if Lorenzo did send the emails without "think[ing] about it one way or the other," as he claims, such a dismissive attitude toward investors' interests would be equally troubling and still constitute acting with extreme recklessness.

D. Lorenzo "made" the material misstatements in the emails.

Lorenzo argues that even if he knowingly sent the materially misleading emails to customers, he cannot

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[26] Lorenzo argues that the Division failed to introduce any expert testimony that would establish the proper standard of care for investment bankers conducting placements of debentures or that would establish that Lorenzo acted recklessly in not catching W2E's write down of its assets. But we need not rely on expert testimony when determining such legal questions. *Cf. Dearlove v. SEC*, 573 F.3d 801, 804 (D.C. Cir. 2009) (stating that "the SEC need not have received expert testimony to establish the standard of care or to determine whether Dearlove's conduct was unreasonable"); *Richard G. Cody*, Exchange Act Release No. 64565, 2011 WL 2098202, at *17 (May 27, 2011) (stating that the Commission is not hindered by the lack of expert testimony when determining whether a securities violation has occurred).

be a primary violator of the antifraud provisions because he did not "make" the misstatements at issue. In support, Lorenzo cites the Supreme Court's decision in *Janus Capital Group v. First Derivative Traders*, which interpreted Rule 10b-5(b)'s prohibition against "mak[ing] any untrue statement of a material fact" as extending only to those with "ultimate authority" over an alleged false statement.[27] This argument is doubly flawed.

As a preliminary matter, because the language that a primary violator must "make" a misstatement appears in only Rule 10b-5(b), the Division need not establish that a defendant "made" a misstatement to establish liability under the other antifraud provisions.[28] And as to Rule 10b-5(b), we conclude that Lorenzo "made" each misstatement by exercising "ultimate authority over the statement, including its content and whether and how to communicate it."[29] Although Lorenzo's emails stated that he was summarizing several key points of the debenture offering at Gregg Lorenzo's "request," Lorenzo testified during his investigatory testimony that he did not recall ever discussing either of the emails or their subject matter with Gregg Lorenzo. Lorenzo later testified at the hearing that he "got the e-mail addresses from [Gregg Lorenzo]," but that, "[i]f memory serves me—I think I authored [the email] and then it was approved by Gregg and Mike [Molinario, Charles'

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[27] 131 S. Ct. 2296, 2302–05 (2011).

[28] *See Flannery*, 2014 WL 7145625, at *10–19.

[29] *Janus*, 131 S. Ct. at 2302.

Vista's compliance officer]." Lorenzo also put his own name and direct phone number at the end of the emails, and he sent the emails from his own account.[30] Lorenzo further testified that he understood that Gregg Lorenzo wanted the emails to come from the investment banking division (which Lorenzo oversaw) and that, by sending the emails, Lorenzo was putting his own reputation on the line.[31]

On appeal, Lorenzo disputes that he was a "maker" of the emails by asserting that he "merely helped to distribute the statements by sending the email that Gregg Lorenzo drafted." Yet there is no persuasive evidence of that. At best, Lorenzo provided conflicting and ambiguous testimony about his and Gregg Lorenzo's respective roles in the emails. For example, when asked during the hearing whether he knew it was

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[30] *Cf. City of Roseville Employees Ret. Sys. v. Energysolutions, Inc.*, 814 F. Supp. 2d 395, 417 (S.D.N.Y. 2011) (stating that there was "no dispute" that each of the defendants who had signed the misstatements had "made" the statements under *Janus*); *S.W. Hatfield, CPA*, Exchange Act Release No. 73763, 2014 WL 6850921, at *6 (Dec. 5, 2014) (finding that respondents had "made" the misstatements where they "drafted, dated, printed on Firm letterhead, and signed" the documents containing the misstatements).

[31] *Cf. Janus*, 131 S. Ct. at 2302 (stating that "attribution within a statement or implicit from surrounding circumstances is strong evidence" that the statement "was made by" the party to whom it was attributed); *SEC v. Greystone Holdings, Inc.*, No. 10-Civ-1302, 2012 WL 1038570, at *9 (S.D.N.Y. Mar. 28, 2012) (finding that chief operating officer was the "maker" of misstatements in certain press releases under *Janus* despite defendant's claim that the chief executive officer had ultimate authority over issuance of press releases).

misleading to tell customers that W2E had $10 million in confirmed assets, Lorenzo testified that he "just made a mistake and sent it. I cut and pasted and sent it. I made a mistake." Lorenzo later testified that, "as soon as [Gregg Lorenzo] gave me the e-mail address, I typed it into the 'to' column and cut and pasted this – the content and sent it out." Lorenzo also claimed, "My boss asked me to send these e-mails out and I sent them out." But all that this self-serving testimony establishes is that Gregg Lorenzo may have asked Lorenzo to email certain customers about the debenture offering and that he provided Lorenzo with the email addresses to do so. It does not establish that anyone other than Lorenzo was ultimately responsible for the emails' content. Nor do the emails themselves establish this. They state only that Gregg Lorenzo had requested that Lorenzo's investment banking division summarize the debenture offering, not that Gregg Lorenzo wrote or had anything else to do with the substance of that summary. To the contrary, Lorenzo testified at the hearing that he remembered authoring the emails himself. And during his earlier investigative testimony, Lorenzo testified that he did not recall ever discussing the emails or their subject matter with Gregg Lorenzo. We therefore find that Lorenzo was ultimately responsible for the emails' content and dissemination and was thus the maker of the misstatements within the meaning of Rule 10b-5(b).[32]

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[32] Although the law judge found that "Gregg Lorenzo had drafted [the emails] relating to the debenture offering to two Charles Vista clients," she did so after weighing the evidence, rather than after making a credibility determination. And even if she had made a credibility finding, we do not accept such findings "blindly." *Ofirfan Mohammed Amanat*, Exchange Act Release No. 54708, 2006 WL

E. Lorenzo's role in the misrepresentation constituted a deceptive "device," an "artifice to defraud," and a deceptive "act" in violation of Section 10(b), Rule 10b-5(a) and (c), and Section 17(a)(1).

We also find that Lorenzo employed a "device, scheme, or artifice to defraud," in violation of Section 17(a)(1) and Rule 10b-5(a); that he engaged in an "act" that would operate as a fraud in violation of Rule 10b-5(c); and that his conduct was deceptive, as required by Section 10(b). Independently of whether Lorenzo's involvement in the emails amounted to "making" the misstatements for purposes of Rule 10b-5(b), he knowingly sent materially misleading language from his own email account to prospective investors. Lorenzo's role in producing and sending the emails constituted employing a deceptive "device," "act," or "artifice to defraud" for purposes of liability under Section 10(b), Rule 10b-5(a) and (c), and Section 17(a)(1).[33]

3199181, at *8 n.46 (Nov. 3, 2006) (noting that "'there are circumstances where, in the exercise of our review function, we must disregard explicit determinations of credibility'" (quoting *Kenneth R. Ward*, Securities Act Release No. 8210, (Mar. 19, 2003) *aff'd*, 75 F. App'x 320 (5th Cir. 2003))), *pet. denied*, 269 F. App'x 217 (3d Cir. 2008); *see also supra* note 35 and accompanying text (describing our *de novo* review).

[33] *See Flannery*, 2014 WL 7145625, at *12–13 (concluding that Rule 10b-5(a) and (c) and Section 17(a)(1) encompass drafting or devising, in addition to "making," a fraudulent misstatement); *accord SEC v. Clark*, 915 F.2d 439, 448 (9th Cir. 1990) (noting that Rule 10b-5(a) and (c) "provide a broad linguistic frame within which a large number of practices may fit").

F. The Commissions' *de novo* review cures any alleged errors in the initial decision.

In his appeal, Lorenzo challenges the sufficiency of the law judge's findings, arguing that the law judge "simply plugged in the facts from Lorenzo's case into [an] earlier [initial decision, *Gualario & Co., LLC*],[34] when they just don't fit." Among other things, Lorenzo contends that the law judge failed to specify which of the three statements at issue in the present case were false, why they were false, or the basis for finding that Lorenzo acted with scienter. Lorenzo similarly claims that the law judge reached her sanctions determinations by "essentially cut[ting] and pasting the facts of Lorenzo's case into the earlier decision," when, according to Lorenzo, "the acts committed [in *Gualario*] were much more severe and completely dissimilar to the facts in this case." Lorenzo contends that, because the law judge did not make adequate findings, "there is no way the Commission can perform an adequate review of its findings." We disagree. Any alleged deficiencies in the law judge's analysis are of no consequence because our review is *de novo*; the violations we find and the sanctions we impose are based on our own independent review of the record.[35] In particular, we find that notwithstanding differences

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[34] Initial Decision Release No. 452, 2012 WL 627198 (Feb. 14, 2012).

[35] *See* Rule of Practice 411(a), 17 C.F.R. § 201.411(a) ("The Commission may affirm, reverse, modify, set aside or remand for further proceedings, in whole or in part, an initial decision by a hearing officer and may make any findings or conclusions that in its judgment are proper and on the basis of the record.").

between the facts in this case and those in *Gualario*, the record evidence of Lorenzo's own, unique misconduct and the risks he poses to investors establishes both the violations we find and the propriety of the sanctions we impose for all the reasons described herein.

IV.

The law judge imposed the following sanctions against Lorenzo: (i) a bar from associating with an investment adviser, broker, dealer, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization companies and from participating in an offering of penny stock; (ii) an order to cease and desist from committing or causing any violations or future violations of Securities Act Section 17(a), Exchange Act Section 10(b), and Exchange Act Rule 10b-5; and (iii) and a third-tier civil penalty of $15,000. We find that these sanctions are appropriate and necessary to protect the investing public.

A. Barring Lorenzo from the industry is appropriate.

Exchange Act Section 15(b)(6) authorizes the Commission to bar a respondent from association with a broker, dealer, investment adviser, municipal securities dealer, municipal advisor, transfer agent, nationally recognized statistical rating organization, and from participating in an offering of penny stock "if that person has willfully violated any provision of the Exchange Act . . . and the bar is in the public

interest."[36] We find that these elements are met and that an industry-wide bar is appropriate.

1. Lorenzo willfully violated the securities laws.

We first find that Lorenzo's conduct was willful. It is well established that "[a] willful violation under the federal securities laws simply means 'that the person charged with the duty knows what he is doing.'"[37] It is sufficient that the actor "intentionally" or "voluntarily" committed the act that constitutes the violation; he need not also be aware that he is violating one of the securities laws or rules promulgated thereunder.[38] Lorenzo claims that he did not give "much thought" to sending the emails, but there is no dispute that Lorenzo intentionally sent them.

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[36] 15 U.S.C. § 78o(b).

[37] *Johnny Clifton*, Exchange Act Release No. 69982, 2013 WL 3487076, at *11 n.75 (July 12, 2013) (quoting *Wonsover v. SEC*, 205 F.3d 408, 414 (D.C. Cir. 2000)).

[38] *Wonsover*, 205 F.3d at 414; *accord Mathis v. SEC*, 671 F.3d 210, 217 (2d Cir. 2012) (stating that willfulness "means intentionally committing the act which constitutes the violation [and that there] is no requirement that the actor also be aware that he is violating one of the Rules or Acts"); *Jason A. Craig*, Exchange Act Release No. 59137, 2008 WL 5328784, at *4 (Dec. 22, 2008) (stating that a willful violations of the securities laws requires that we "need to find only that [the respondent] voluntarily committed the acts that constituted the violation, not that [the respondent] was aware of the rule he violated or that he acted with a culpable state of mind").

2. An industry-wide bar is in the public interest.

We assess whether a bar is in the public interest by considering the egregiousness of Lorenzo's conduct, the isolated or recurrent nature of the infraction, the degree of scienter involved, Lorenzo's recognition of the wrongful nature of his conduct, the sincerity of any assurances against future violations, and the likelihood that Lorenzo's occupation will present opportunities for future violations.[39] Our inquiry into these factors "is a flexible one, and no one factor is dispositive."[40] Here, these considerations weigh in favor of barring Lorenzo from the industry.

Lorenzo's conduct was egregious. A fundamental purpose of the securities laws is "to substitute a philosophy of full disclosure for the philosophy of caveat emptor and thus to achieve a high standard of business ethics in the securities industry."[41] Because of this, "[t]he proper functioning of the securities industry and markets depends on the integrity of industry participants and their commitment to transparent

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[39] *Ronald S. Bloomfield*, Exchange Act Release No. 71632, 2014 WL 768828, at *18 (Feb. 27, 2014); *accord Steadman v. SEC*, 603 F.2d 1126, 1140 (5th Cir. 1979), *aff'd on other grounds*, 450 U.S. 91 (1981).

[40] *Disraeli*, 2007 WL 4481515, at *15 (quoting *Conrad P. Seghers*, Advisers Act Release No. 2656, 2007 WL 2790633, at *4 (Sept. 26, 2007), *pet. for review denied*, 548 F.3d 129 (D.C. Cir. 2008)), *pet. for review denied*, 334 F. App'x 334 (D.C. Cir. 2009).

[41] *SEC v. Capital Gains Research Bureau*, 375 U.S. 180, 186 (1963).

disclosure."[42] Lorenzo demonstrated a complete disregard for these principles by grossly misleading, if not outright lying to, retail customers about the significant risks involved in purchasing W2E's debentures. We have repeatedly warned that such violations of the antifraud provisions are "'especially serious and subject to the severest of sanctions under the securities laws.'"[43]

Lorenzo has also displayed troubling dishonesty. He sent his two misleading emails separately, to different customers, thus presenting separate opportunities to mislead prospective investors. And while Lorenzo seeks credit for voluntarily testifying to Commission staff during its investigation, his testimony painted a notably misleading picture of his employer and W2E's offering. For example, while Lorenzo initially described Gregg Lorenzo to Commission staff as an "honest guy," he later admitted at the hearing that "there [wa]s no way on God's green earth I thought Gregg Lorenzo was an honest guy." Lorenzo similarly described W2E's debt offering as a high quality project during the investigation but later admitted that he thought the offering was "a toxic convertible debt spiral."

Lorenzo also acted with a high degree of scienter. Lorenzo knew, when he sent his emails to customers,

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[42] *Clifton*, 2013 WL 3487076, at *14 (quoting *John W. Lawton*, Advisers Act Release No. 3513, 2012 WL 6208750, at *11 (Dec. 13, 2012)).

[43] *Peter Siris*, Exchange Act Release No. 71068, 2013 WL 6528874, at *6 (Dec. 12, 2013) (quoting *Vladimir Boris Bugarski*, Exchange Act Release No. 66842, 2012 WL 1377357, at *4 (Apr. 20, 2012)), *pet. for review denied*, 773 F.3d 89 (D.C. Cir. 2014).

that he was misstating critical facts about W2E and the safety of its debenture offering.[44] That Lorenzo so blatantly ignored the importance of communicating truthfully with potential investors creates a significant risk that he will engage in similar misconduct in the future and demonstrates his unfitness to participate in the securities industry.[45]

Lorenzo's unwillingness to accept responsibility for this misconduct further weighs in favor of a bar. Although he claims to have "apologized many times for his limited involvement with the W2E debentures" and to "regret[] the emails being sent out," he continues to blame W2E and Gregg Lorenzo for his actions. Lorenzo claims, for instance, that W2E failed to inform him properly of the $10 million write-down and that he sent the emails at Gregg Lorenzo's direction. But none of these supposed failures by others explains, or excuses,

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[44] *Cf. Jeffrey L. Gibson*, Exchange Act Release No. 57266, 2008 WL 294717, at *3 (Feb. 4, 2008) (stating that respondent's conduct "evince[d] a high degree of scienter" because "he knew [the private placement memorandum]'s representations with respect to the use of proceeds were misleading"), *pet. for review denied*, 561 F.3d 548 (6th Cir. 2009).

[45] *Cf. Tzemach David Netzer Korem*, Exchange Act Release No. 70044, 2013 WL 3864511, at *7 (July 26, 2013) (finding that "the deliberate manner in which Korem flouted [a core] responsibility suggests that he is likely to engage in future misconduct"); *Lawton*, 2012 WL 6208750, at *9 (considering past conduct as evidence in a "broader inquiry into whether a person presents a future risk to the public interest because, as the Supreme Court has recognized, the 'degree of intentional wrongdoing evident in a defendant's past conduct' is an important indication of the defendant's propensity to subject the trading public to future harm" (quoting *Aaron v. SEC*, 446 U.S. 680, 701 (1980))).

Lorenzo's decision to send retail customers emails that he knew contained materially misleading statements. Such a refusal to accept responsibility "has long been deemed an appropriate measure of fitness for association in the industry."[46]

We are particularly troubled by Lorenzo's continued attempts to shift blame onto W2E for not disclosing the company's write down more fully. Lorenzo criticized W2E's supposed lack of disclosure by testifying that the company's $10 million write-down "deserved a Sermon on the Mount meeting" and "needed to be emphasized, emphasized, not minimized and not hidden in a regulatory document." Yet when discussing his own failure to disclose the same write-down to investors, Lorenzo dismissed his conduct as an "unintentional miscue" and his involvement as "limited." Although a respondent has the right to present a vigorous defense, we find that Lorenzo's continued attempts here to shift blame and minimize his role in deceiving investors demonstrate that he "does not fully understand the seriousness of his misconduct and how it violated the duties of a securities professional" and "presents a significant risk that, given th[e] opportunity, he would commit further misconduct in the future."[47]

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[46] *Gregory Bartko*, Exchange Act Release No. 71666, 2014 WL 896758, at *11 (Mar. 7, 2014) (finding that respondent's unwillingness to accept responsibility weighed in favor of a bar); *accord Seghers*, 548 F.3d at 137 (holding that imposition of a more severe sanction for refusal to accept responsibility "did not unconstitutionally burden [respondent] in the district court . . . nor did it deny him due process before the SEC").

[47] *Clifton*, 2013 WL 3487076, at *14 (citations omitted).

Nor does the lack of any demonstrated causal link between Lorenzo's emails and the customers' ultimate investment decisions weigh against a bar. The Division is not required to establish either reliance or loss by any investor.[48] Instead, "our focus is on the welfare of investors generally and the threat one poses to investors and the markets in the future."[49] And that is particularly true here, as Lorenzo's emails created a substantial risk to investors by misleading them about the likelihood of losing much, if not all, of any investment.

We are also unpersuaded by Lorenzo's claim that his occupation will not present opportunities for future violations. Lorenzo contends that his communicating with retail customers "was a unique occurrence that was outside the scope of his investment banking responsibilities—both at Charles Vista and at his [subsequent] firm," but his admission that sending emails to customers was not within his normal duties heightens our concern that Lorenzo will engage in future misconduct if allowed to remain in the industry, no matter the scope of that employment. As we have repeatedly observed, "[t]he securities industry presents continual opportunities for dishonesty and abuse, and

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[48] *See, e.g.*, *Morgan Keegan & Co.*, 678 F.3d at 1244; *Graham v. SEC*, 222 F.3d 994, 1001 n.15 (D.C. Cir. 2000).

[49] *Gary M. Kornman*, Exchange Act Release No. 59403, 2009 WL 367635, at *9 (Feb. 13, 2009) (citing *Christopher A. Lowry*, Advisers Act Release No. 2052, 55 SEC 1133, 2002 WL 1997959, at *6 (Aug. 30, 2002), *aff'd*, 340 F.3d 501 (8th Cir. 2003)); *cf. Korem*, 2013 WL 3864511, at *5 (rejecting respondent's argument that his conduct was not egregious because there was no harm or loss).

depends heavily on the integrity of its participants and on investors' confidence."[50] And the antifraud provisions that Lorenzo violated apply to all securities industry participants. While we recognize the severity of a collateral bar and its obvious impact on Lorenzo's ability to continue working in the securities industry, we find, for all the reasons discussed herein, that imposing such a bar on Lorenzo from associating with any investment adviser, broker, dealer, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization and from participating in an offering of penny stocks is necessary to prevent Lorenzo from putting investors at further risk and will deter other market professionals from engaging in similar misconduct.[51]

Lorenzo argues that imposing such a bar is so "grossly disproportionate to the offense at issue, particularly given Mr. Lorenzo's long unblemished career in the securities industry," that it violates the Eighth Amendment's prohibition against excessive punishment. We disagree. Although some mitigating

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[50] *Seghers*, 2007 WL 2790633, at *7; *see also Koch*, 2014 WL 1998524, at *21 n.224 (citing cases).

[51] *Cf. Lawton*, 2012 WL 6208750, at *12–13 (finding that a collateral bar was justified when respondent "reveal[ed] an attitude toward regulatory oversight that is fundamentally incompatible with the principles of investor protection"; violated professional responsibilities that are "not limited to a particular aspect of the securities industry"; and demonstrated "his ongoing unfitness and risk that he would engage in further misconduct if given future opportunities in the industry," where "opportunities for similar misconduct arise in each of the associational capacities covered by the collateral bar").

factors exist, including that Lorenzo has a relatively clean disciplinary record, that he claims to have made some effort at assisting defrauded investors, and that he earned relatively little profit from his misconduct, his claims of mitigation are far outweighed by the gravity of his violations and the risk of his committing future violations.[52] Our intent in ordering that Lorenzo be barred from the industry is to protect the investing public from further harm, not to punish Lorenzo.[53] And the Exchange Act specifically authorizes us to impose such an industry-wide bar.[54] Barring him from the

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[53] *Cf. Philip J. Milligan*, Exchange Act Release No. 61790, 2010 WL 1143088, at *5 (Mar. 26, 2010) (imposing an associational bar despite a previously clean record); *Terrance Yoshikawa*, Exchange Act Release No. 53731, 2006 WL 1113518, at *8 (Apr. 26, 2006) (sustaining self-regulatory organization's imposition of a bar because, while the petitioner earned "a relatively small amount of profits," the potential harm to the markets "could be considerably greater than this dollar amount"); ***Marshall E. Melton***, Exchange Act Release No. 48228, 56 SEC 695, 2003 WL 21729839, at *7 (July 25, 2003) (finding that respondent's previously clean record did not outweigh his misconduct and imposing a bar). We also note that Lorenzo's disciplinary history is not quite unblemished, as Lorenzo claims. In June 2011, FINRA suspended Lorenzo for twelve days in all capacities for failing to timely pay outstanding FINRA hearing session fees. *See* http://brokercheck.finra.org (last visited April 28, 2015).

[54] *McCarthy v. SEC*, 406 F.3d 179, 188 (2d Cir. 2005); *cf. Seghers*, 2007 WL 2790633, at *9 (stating that imposition of a bar was "not intended to punish, but 'to protect the public interest from future harm at his hands'" (quoting *Leo Glassman*, Exchange Act Release No. 11929, 46 SEC 209, 1975 WL 160418, at *2 (Dec. 16, 1975))), *pet. for review denied*, 548 F.3d 129 (D.C. Cir. 2008).

[55] *Cf. Eric J. Brown*, Exchange Act Release No. 66469, 2012 WL 625874, at *18 (Feb. 27, 2012) (observing that substantial

industry is therefore not a punishment within the meaning of the Eighth Amendment.[55]

At oral argument, Lorenzo's counsel asserted that imposing an industry-wide bar would be inconsistent with the one-year suspension that we imposed against respondents in *John P. Flannery*.[56] But the Commission has consistently held that the "appropriate sanction depends upon the facts and circumstances of each particular case and cannot be determined precisely by comparison with actions taken in other proceedings."[57] And here, although Lorenzo and the respondents in *Flannery* all had relatively clean disciplinary histories, we find that the egregiousness of Lorenzo's misstatements, the high degree of his scienter, and his continued attempts to shift blame onto others, along with the other considerations discussed above, are distinguishable from *Flannery* and warrant a bar in this case. This conclusion is consistent with our repeated holding "that conduct that violates

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deference is granted to the legislature when determining whether a penalty is excessive under the Eighth Amendment).

[55] *Cf. Charles Phillip Elliot*, Exchange Act Release No. 31202, 50 SEC 1273, 1992 WL 258850, at *4 (Sept. 17, 1992) (finding that a bar from the industry is not a punishment within the meaning of the Eighth Amendment (citing *Flemming v. Nestor*, 363 U.S. 603, 613–14 (1960))).

[56] 2014 WL 7145625, at *10.

[57] *Ronald Pellegrino*, Exchange Act Release No. 59125, 2008 WL 5328765, at *17 n.68 (Dec. 19, 2008) (quoting *Christopher J. Benz*, Exchange Act Release No. 38440, 52 SEC 1280, 1997 WL 137027, at *4 (March 26, 1997), *petition denied*, 168 F.3d 478 (3d Cir. 1988) (Table)).

the antifraud provisions of the securities laws is especially serious and subject to the severest of sanctions under the securities laws."[58]

B. Ordering Lorenzo to cease and desist from violating the antifraud provisions is in the public interest.

Securities Act Section 8A(a) and Exchange Act Section 21C(a) authorize us to issue a cease-and-desist order against any person who "has violated" those statutes or rules thereunder.[59] When determining whether such an order is appropriate, we consider public interest factors that are substantially the same as those we consider when assessing whether to impose a bar.[60] "In addition, we consider whether the violation is recent, the degree of harm to investors or the marketplace resulting from the violation, and the remedial function to be served by the cease-and-desist order in the context of any other sanctions being

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[58] *Siris*, 2013 SEC LEXIS 3924, at *23 (imposing a full collateral bar); *see also Clifton*, 2013 WL 3487076, at *14 (same).

[59] 15 U.S.C. § 77h-1(a) (Securities Act); *id.* § 78u-3(a) (Exchange Act).

[60] *See Joseph J. Barbato*, Exchange Act Release No. 41034, 53 SEC 1259, 1999 WL 58922, at *14 n.31 (Feb. 10, 1999). For instance, we consider the seriousness of the violation, the isolated or recurrent nature of the violation, the respondent's state of mind in committing the violation, the sincerity of assurances against future violations, the respondent's recognition of the wrongful nature of the conduct, and the respondent's opportunity to commit future violations. *KPMG Peat Marwick LLP*, Exchange Act Release No. 43862, 54 SEC 1135, 2001 WL 47245, at *26 (Jan. 19, 2001), *pet. for review denied*, 289 F.3d 109 (D.C. Cir. 2002).

sought."[61] This inquiry is flexible, and no single factor is dispositive.[62] "Absent evidence to the contrary, a finding of violation raises a sufficient risk of future violation."[63]

As discussed above, Lorenzo's conduct was egregious, demonstrated a pattern of dishonesty, evidenced a high degree of scienter, and presents a substantial risk of future violations.[64] Lorenzo's clear failure to appreciate his responsibilities as a securities professional outweighs the various factors Lorenzo asserts as mitigating: that his misconduct occurred approximately five years ago; that he claims to "regret[] the emails being sent out"; that, after leaving Charles Vista, he claims to have spent "a substantial amount of time and effort assisting investors who purchased W2E debentures in organizing and filing claims"; and that he claims to have given "statements to the Commission,

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[61] *KPMG Peat Marwick*, 2001 WL 47245, at *26.

[62] *Id.*

[63] *Id.* at *24 (finding that a cease-and-desist order may be imposed only where there is some risk of future violations, but that the risk "need not be very great"); *see also Schoemann v. SEC*, 398 F. App'x 603, 604 (D.C. Cir. 2010) (per curiam) (affirming the imposition of a cease-and-desist order because petitioner's conduct "constituted a violation of the [Securities] Act"), *aff'g* Securities Act Release No. 9076, 2009 WL 3413043, at *12–13 (Oct. 23, 2009) (noting that "absent evidence to the contrary, a single past violation ordinarily suffices to raise a sufficient risk of future violations").

[64] *See supra* notes 42–51 and accompanying text; *cf. Gregory O. Trautman*, Exchange Act Release No. 61167A, 2009 WL 6761741, at *21 (Dec. 15, 2009) (imposing cease-and-desist order for violations that "involved a high degree of scienter").

without retaining a lawyer, for the purpose of aiding the Commission, and particularly those who purchased W2E debentures."[65]

Moreover, although we are ordering that Lorenzo be barred from serving in the securities industry, he could still rejoin the industry in a non-registered capacity or otherwise become active in the financial markets. Our concern that Lorenzo will commit future violations, regardless of any constraints placed on his involvement in the industry, is heightened by Lorenzo's acknowledgement that he sent the emails outside the scope of his investment banking responsibilities. Ordering Lorenzo to cease and desist from violating the antifraud provisions will serve the remedial purpose of encouraging Lorenzo to take his responsibilities more seriously should he be allowed to re-enter the securities industry or should he resume acting in a capacity that does not require registration.[66]

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[65] Lorenzo testified that, after he left Charles Vista, "a lot of clients, they didn't want to speak to Gregg [Lorenzo] anymore, so he would toss them to me." At which point, Lorenzo explained, "I got to know a few of these debentures holders, about 15." He said that he told them: "'My suggestion is this, you form a group and you try and get some relief as a group from either Waste2Energy or Charles Vista.' I did this—I didn't charge him money to help. I just made the introduction."

[66] *Cf. Trautman*, 2009 WL 6761741, at *21 (finding a cease-and-desist order to be appropriate where the Commission also imposed a bar).

C. Imposing a civil penalty of $15,000 is in the public interest.

Securities Act Section 8A(g) and Exchange Act Section 21B(a) authorize us to impose civil monetary penalties for violations of those securities statutes if it is in the public interest and if, in the case of Exchange Act § 21B(a), the respondent willfully violated the Exchange Act.[67] As discussed above, Lorenzo acted willfully when committing his violations. The question is therefore whether a civil penalty is in the public interest, which we assess based on (i) whether the act or omission involved fraud or deliberate or reckless disregard of a regulatory requirement; (ii) whether the act or omission resulted in harm to others; (iii) the extent to which any person was unjustly enriched, taking into account restitution made to injured persons; (iv) whether the individual has committed previous violations; (v) the need to deter such person and others from committing violations; and (vi) such other matters as justice may require.[68]

We find that these factors weigh in favor of imposing a monetary sanction. We acknowledge Lorenzo's relative lack of disciplinary history, that the amount of his gain was relatively small ($150), and that there was no evidence that his conduct directly led to significant customer losses. But none of this

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[67] 15 U.S.C. §§ 77h-1 (providing that the Commission may impose civil penalties if it finds a violation of the Securities Act in a cease-and-desist proceeding), 78u-2 (providing that the Commission may impose civil penalties for any violation of the federal securities laws).

[68] *Id.* § 78u-2(c).

outweighs that Lorenzo displayed a knowing and reckless disregard for his obligations as a securities professional by sending materially misleading emails to retail customers. The need to deter Lorenzo from committing such deliberately fraudulent conduct in the future warrants imposition of a monetary sanction.

As for the amount of that sanction, the securities laws authorize us to impose first-tier penalties of up to $6,500 for each "act or omission"; second-tier penalties of up to $65,000 for each act or omission that "involved fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement"; and third-tier penalties of up to $130,000 for each act or omission that "resulted in substantial losses," created "a significant risk of substantial losses to other persons," or resulted in "substantial pecuniary gain to the person who committed the act or omission."[69]

Here, we find that Lorenzo committed two "acts or omissions" in violation of the securities laws by sending two different customers a materially misleading email.[70] While the emails he sent were largely the same and sent close in time, they were not identical and provided Lorenzo two separate opportunities to mislead customers. As for the appropriate sanction for each act or omission, we find that a third-tier penalty is appropriate because Lorenzo's violations involved

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[69] *Id.* §§ 77h-1(g)(2), 78u-2(b); *see also* 17 C.F.R. § 201.1003 (setting forth the maximum penalty amounts for violations occurring from February 15, 2005 to March 3, 2009).

[70] *Cf. SEC v. Pentagon Capital Mgmt. PLC*, 725 F.3d 279, 288 n.7 (2d Cir. 2013) (finding no error in a district court counting each late trade as a separate violation).

"fraud, deceit, [and] deliberate or reckless disregard of a regulatory requirement," while also creating "a significant risk of substantial losses" to the customers.[71] Specifically, Lorenzo hid the fact that W2E was in dire financial straits and that the customers were unlikely to recoup much, if any, of their investment in the event of default. This deceit created a significant risk that recipients of the emails would lose all of whatever they decided to invest. That the customers were ultimately unable, or unwilling, to invest more than $15,000 does not negate the possibility that Lorenzo's misleading emails could have resulted in far larger investments (and subsequent losses). After all, Lorenzo was seeking to raise $15,000,000 for W2E. Such a risk of substantial loss warrants imposition of the highest tier penalty, regardless of whether either customer actually read or relied on Lorenzo's emails when making their investment decision.[72]

We nevertheless recognize Lorenzo's relative lack of profit, the lack of evidence that the emails harmed others, and Lorenzo's relatively clean disciplinary record. While we do not believe these mitigating factors outweigh the need to protect investors from future harm by barring him from the industry, we nevertheless decline to grant the Division's request to impose a $100,000 civil penalty. We instead find that a

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[71] 15 U.S.C. §§ 77h-1(g)(2), 78u-2(b).

[72] *Cf. Clifton*, 2013 WL 3487076, at *16 (imposing a maximum third tier penalty where the respondent had sought to raise more than $1 million, but where the record contained no evidence regarding actual losses nor substantial pecuniary gains).

third-tier penalty of $7,500 for each of Lorenzo's emails (for an aggregate of $15,000) is in the public interest to deter Lorenzo and others in similar positions from committing future violations.

An appropriate order will issue.[73]

By the Commission (Chair WHITE and Commissioners AGUILAR and STEIN; Commissioners GALLAGHER and PIWOWAR concurring in part and dissenting with respect to the bars from association with municipal advisors and nationally recognized statistical rating organizations).

Brent J. Fields
Secretary

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[73] We have considered all of the parties' contentions. We have rejected or sustained them to the extent that they are inconsistent or in accord with the views expressed in this opinion.

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 9762 / April 29, 2015

SECURITIES EXCHANGE ACT OF 1934
Release No. 74836 / April 29, 2015

Admin. Proc. File No. 3-15211

[Filed XXX]

In the Matter of	)
	)
FRANCIS V. LORENZO	)
c/o Robert G. Heim	)
Meyers & Heim LLP	)
444 Madison Ave., 30th Floor	)
New York, NY 10022	)
	)

ORDER SUSTAINING DISCIPLINARY ACTION

On the basis of the Commission's opinion issued this day, it is

ORDERED that Francis V. Lorenzo be barred from association with any broker, dealer, investment adviser, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization and from participating in an offering of penny stocks; and it is further

ORDERED that Francis V. Lorenzo cease and desist from committing or causing any violations or future violations of Section 17(a)(1) of the Securities Act of

1933 and Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder; and it is further

ORDERED that Francis V. Lorenzo pay a civil money penalty in the amount of $15,000.

Payment of the civil money penalty shall be: (i) made by U.S. postal money order, certified check, bank cashier's check, or bank money order; (ii) made payable to the Securities and Exchange Commission; (iii) mailed or delivered by hand to the Office of Financial Management, Securities and Exchange Commission, 100 F. Street NE, Mail Stop 6042, Washington, DC 20549; and (iv) submitted under cover letter that identifies the respondent and the file number of this proceeding. A copy of the cover letter and check shall be sent to Alex Janghorbani and Jack Kaufman, Division of Enforcement, U.S. Securities and Exchange Commission, New York Regional Office, Brookfield Place, 200 Vesey Street, Suite 400, New York, NY, 10281.

Brent J. Fields
Secretary

APPENDIX C

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FILE NO. 3-15211

[Filed December 31, 2013]

In the Matter of	)
	)
GREGG C. LORENZO,	)
FRANCIS V. LORENZO, and	)
CHARLES VISTA, LLC	)
	)

INITIAL DECISION RELEASE NO. 544
ADMINISTRATIVE PROCEEDING
FILE NO. 3-15211

INITIAL DECISION AS TO FRANCIS V. LORENZO[1]

December 31, 2013

APPEARANCES:

Alex Janghorbani and Jack Kaufman for the Division of Enforcement, Securities and Exchange Commission

Robert J. Hantman of Hantman & Associates for Respondent Francis V. Lorenzo

BEFORE:

Carol Fox Foelak, Administrative Law Judge

SUMMARY

This Initial Decision (ID) concludes that Respondent Francis V. Lorenzo (Frank Lorenzo or Respondent) violated the antifraud provisions of the federal securities laws when he sent two potential investors emails containing false and misleading information about his firm's client. The ID orders him to cease and

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[1] The proceeding has ended as to Respondents Gregg C. Lorenzo and Charles Vista, LLC, who settled the charges against them. Gregg C. Lorenzo, Securities Act Release No. 9480, 2013 WL 6087352 (Nov. 20, 2013) (Settlement Order). The Settlement Order made various findings, including findings that Francis V. Lorenzo (Frank Lorenzo) engaged in various conduct, including conduct concerning which there was no evidence at Frank Lorenzo's hearing on September 18-19, 2013. It must be stressed that the only basis on which the undersigned or the Securities and Exchange Commission may evaluate Frank Lorenzo's conduct in this proceeding is the evidence adduced at his September 18-19, 2013, hearing.

desist from violations of the antifraud provisions, bars him from the securities industry, and orders him to pay a civil money penalty of $15,000.

I. INTRODUCTION

A. Procedural Background

The Commission instituted this proceeding with an Order Instituting Proceedings (OIP) on February 15, 2013, pursuant to Section 8A of the Securities Act of 1933 (Securities Act) and Sections 15(b), 21B, and 21C of the Securities Exchange Act of 1934 (Exchange Act). The undersigned held a two-day hearing in New York City on September 18-19, 2013. Three witnesses testified, including Frank Lorenzo, and numerous exhibits were admitted into evidence.[2]

The findings and conclusions in this ID are based on the record. Preponderance of the evidence was applied as the standard of proof. See Steadman v. SEC, 450 U.S. 91, 97-104 (1981). Pursuant to the Administrative Procedure Act, 5 U.S.C. § 557(c), the parties' Proposed Findings of Fact and Conclusions of Law[3] were considered. All arguments and proposed findings and conclusions that are inconsistent with this ID were considered and rejected.

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[2] Citations to the transcript will be noted as "Tr. __." Citations to exhibits offered by the Division of Enforcement (Division) and by Respondent will be noted as "Div. Ex. __" and "Resp. Ex. __," respectively.

[3] Reference to the Division's and Respondent's Proposed Findings of Fact and Conclusions of Law will be noted as "Div. Br." and "Resp. Br.," respectively.

B. Allegations and Arguments of the Parties

This proceeding concerns Frank Lorenzo's dealings with customers of Charles Vista, LLC (Charles Vista), a registered broker-dealer owned by Gregg C. Lorenzo (Gregg Lorenzo), during the fall of 2009. The OIP alleges that Lorenzo sent at least two Charles Vista customers emails containing false and misleading statements concerning the assets and business of Waste2Energy Holdings, Inc. (W2E), a start-up waste management company for which Charles Vista was attempting to sell convertible debentures.

The Division of Enforcement (Division) is seeking a cease-and-desist order, a third-tier civil money penalty, and a bar. Respondent argues that the charges are unproven and no sanctions should be imposed.

II. FINDINGS OF FACT

As discussed below, on October 14, 2009, Frank Lorenzo sent two potential investors emails that contained false and misleading information about W2E.

A. Relevant Individuals and Entities

1. Charles Vista, Gregg Lorenzo, and Frank Lorenzo

Charles Vista was a registered broker-dealer that Gregg Lorenzo owned and operated since 2009.[4] Tr.

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[4] According to Financial Industry Regulatory Authority, Inc. (FINRA), records, Charles Vista withdrew its registration as a broker-dealer on June 17, 2013. Additionally, FINRA cancelled Charles Vista's membership on July 31, 2013, for failure to pay outstanding fees. See http://brokercheck.finra.org (last visited

291; Div. Ex. 132 at 13. Charles Vista and Gregg Lorenzo have settled the charges against them in this proceeding. See Gregg C. Lorenzo, Securities Act Release No. 9480 (Nov. 20, 2013), 2013 WL 6087352 (Settlement Order). According to the Settlement Order, Gregg Lorenzo engaged in numerous fraudulent activities in connection with the business of Charles Vista. His previous ten years as a registered representative, associated with various broker-dealers, were studded with disciplinary issues.[5]

Frank Lorenzo has worked in the securities industry for over twenty-five years. Tr. 185-90; Div. Ex. 25; Resp. Ex. 1 at 4-5. In 2007, he joined Mercer Capital, Ltd. (Mercer Capital), where he was the firm's investment banker.[6] Tr. 187-89; Div. Ex. 25; Resp. Ex. 1 at 4-5. There, he met Gregg Lorenzo. Tr. 304-05; Div. Ex. 132 at 11-13. Frank Lorenzo and Gregg Lorenzo are not related. Tr. 305. Frank Lorenzo followed Gregg Lorenzo to John Thomas Financial, Inc.,

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Dec. 3, 2013). Official notice, pursuant to 17 C.F.R. § 201.323, is taken of these records. See Joseph S. Amundsen, Exchange Act Release No. 69406 (Apr. 18, 2013), 2013 SEC Lexis 1148, at *2 n. 1.

[5] According to FINRA records, FINRA permanently barred Gregg Lorenzo from association with any member, effective November 14, 2013, for his refusal to comply with multiple requests to appear for an on-the-record interview; the records also indicate an extensive state disciplinary record, including by the states of Idaho, Iowa, and Montana. See http://brokercheck.finra.org (last visited Dec. 3, 2013).

[6] According to FINRA records, Mercer Capital, Ltd, terminated or withdrew its membership as of January 15, 2010. See http://brokercheck.finra.org (last visited Dec. 3, 2013).

and then, when he found that firm too stressful, to Charles Vista, in February 2009. Tr. 181, 189-90; Div. Ex. 25 at 1; Resp. Ex. 1 at 4-5.

At Charles Vista, Frank Lorenzo was the director of investment banking. Tr. 66, 89, 181, 403; Div. Ex. 25 at 1. By the summer of 2009, Frank Lorenzo knew that Charles Vista was a "boiler room," as his assistant told him that the firm's brokers were engaged in high-pressure sales and stretching the truth to clients, and by the fall of 2009, he doubted the prudence of how Charles Vista handled clients' money. Tr. 229-30, 291-92, 299-302, 323-24, 383, 404-05. He left Charles Vista in February 2010, and has continued to work in the securities industry, currently at Hunter Wise Securities, LLC, a registered broker-dealer. Tr. 181, 311; Div. Ex. 25 at 1; Resp. Ex. 1 at 4. During the time he worked at Charles Vista, Frank Lorenzo was paid about $120,000 but incurred expenses of $60,000 to $80,000 for which he was promised, but did not receive, reimbursement. Tr. 297-98. Except for the events at issue, Frank Lorenzo has had no disciplinary issues as a registered representative. Tr. 336-37.

2. Waste2Energy Holdings, Inc. (W2E)

W2E is central to the events at issue. Tr. passim; Div. Exs. passim. W2E was a renewable energy company, founded in 2007 and made public in early 2009, which engaged Charles Vista for investment banking support. Tr. 42, 66, 77-78, 141; Div. Ex. 3 at 3. In September 2009, W2E was preparing to offer up to $15 million in 12% convertible debentures, and Charles Vista was the placement agent for this offering. Tr. 85-89; Div. Ex. 1 at page 19 of 112; Div. Ex. 3. As placement agent for the offering, Charles Vista was

positioned to earn substantial fees, including a 10% commission on sales of the debentures. See Div. Ex. 3 at iii.

W2E was in terrible financial shape during Frank Lorenzo's time at Charles Vista. Tr. 198-99. W2E's technology – aimed at converting solid waste into electricity – did not work. Tr. 42, 190, 199; see Div. Ex. 3 at 3, 21-22 (describing what the company does). W2E was placed into bankruptcy in 2012. Tr. 96, 139-40, 387; Div. Ex. 53 at 3-4.

Part of Frank Lorenzo's job as Charles Vista's head of investment banking was to conduct due diligence of investment banking clients, such as W2E, which included reviewing their filings with the Commission. Tr. 182-83, 197-98, 231-32. As Charles Vista's investment banker, Frank Lorenzo was responsible for overseeing the W2E relationship, and he was W2E's primary point of contact at Charles Vista. Tr. 65-66, 95, 155, 327-28. Indeed, the majority of Frank Lorenzo's responsibilities at Charles Vista related to W2E. Tr. 197.

B. W2E Asset Write-Off

On June 3, 2009, W2E filed a Form 8-K that contained unaudited financial statements as of December 31, 2008; the balance sheet listed about $14 million in total assets, which included about $10 million in "intangibles," and about $470,000 in "goodwill." Tr. 57, 201; Div. Ex. 15[7] at page 63 of 175. The intangibles figure referred to the valuation assigned to the company's intellectual property

[7] W2E was previously known as Maven Media Holdings. Tr. 54-55.

(essentially the technology to turn waste into energy), and the goodwill figure referred to the valuation assigned to the company's workforce. Tr. 56-57. Frank Lorenzo reviewed this Form 8-K in June 2009. Tr. 121.

W2E filed an amended Form 8-K (8-K/A) on October 1, 2009, with audited March 31, 2009, fiscal year-end financial statements. Tr. 58, 227; Div. Ex. 16. The balance sheet for the year ended March 31, 2009, reported no intangibles; following months of auditing work by W2E's independent accountants, the company had written the intangibles down to zero. Tr. 59-60, 69; Div. Ex. 16 at pages 46, 69 of 137. W2E also had written down the value of the goodwill to zero. Tr. 60, 70. With these substantial supposed assets entirely written down, the Form 8-K/A ultimately reflected under $370,600 in audited total assets for the year ended March 31, 2009 – i.e., under 3% of the total assets reflected in the December 31, 2008, balance sheet. Compare Div. Ex. 16 at page 69 of 137 with Div. Ex. 15 at page 63 of 175.

Also on October 1, 2009, W2E filed a Form 10-Q. Tr. 58, 67; Div. Ex. 22. This Form 10-Q, for the quarterly period ended June 30, 2009, again did not list any intangibles, and listed audited total assets under $370,600 for the year ended March 31, 2009. Div. Ex. 22 at page 4 of 45. It further listed audited total liabilities of over $6.6 million for the year ended March 31, 2009. Id.

On October 1, 2009, Frank Lorenzo reviewed both the Form 8-K/A and the Form 10-Q filed on that day. Tr. 231, 241; Div. Ex. 32. Indeed, he shared the filings with all brokers at Charles Vista early on October 2. Tr. 233, 243; Div. Ex. 21. October 2009, however, was

not the first time Frank Lorenzo had heard about the write-off of the majority of W2E's claimed assets; he had known about the write-off at least since the prior month. Tr. 116, 144, 154-55, 220-21; Div. Ex. 18. Furthermore, prior to October 2009, Frank Lorenzo had speculated that the intangibles were not in fact worth close to the $10 million W2E has previously claimed. Tr. 268. Frank Lorenzo believed that the amount written off was material, and thought the fact of the write-off was a "big deal." Tr. 216-17, 231, 243-44.

Following his receipt of the Forms 8-K/A and 10-Q, and prior to October 14, 2009, Frank Lorenzo was involved in a discussion between Charles Vista and W2E regarding the asset write-off. Tr. 74-77, 122-23, 249-51; Div. Exs. 19, 42.

C. The Two Emails

On October 14, 2009, Gregg Lorenzo asked Frank Lorenzo to send an email that Gregg Lorenzo had drafted relating to the debenture offering to two Charles Vista clients – William Rothe (Rothe) and Vishal Goolcharan (Goolcharan) – saying that he wanted the emails to come from Charles Vista's investment banking division. Tr. 173, 257-59, 264, 343-44, 346, 381-82; Div. Ex. 49. Frank Lorenzo heeded Gregg Lorenzo's instruction without question, sending an almost identical email to each client on that day.[8]

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[8] The email to Goolcharan states that it was sent at the request of Adam Spero and Gregg Lorenzo, while the email to Rothe states that it was sent at the request of Gregg Lorenzo.

Tr. 176-77, 257-58, 341, 346, 378, 381-82, 403-04; Div. Ex. 34. The email read in full:

> Dear Sir:
>
> At the request of Adam Spero and Gregg Lorenzo, the Investment Banking division of Charles Vista has summarized several key points of the Waste2Energy Holdings, Inc. Debenture Offering.
>
> *** Please read the Offering Memorandum, including all "Risk Factors" ***
>
> 12- month Note, Debenture pays a 12% interest rate, paid quarterly
>
> A sinking fund has been created, handled by 3rd party (SRFF attorney). Interest payment amount will be held in the sinking fund
>
> This is senior debt. There is no other debt (other than simple debt). These debenture holders have to approve (51%) any other debt.
>
> If there is a liquidation, these debenture holders get paid first.
>
> <u>There are 3 layers of protection:</u>
>
> > <u>(I) The Company has over $10 mm in confirmed assets</u>
> > <u>(II) The Company has purchase orders and LOI's for over $43 mm in orders</u>
> > <u>(III) Charles Vista has agreed to raise additional monies to repay these Debenture holders (if necessary)</u>

Debenture Holders have the option to convert their debt at $1.00 into common stock. These shares would have been already added to the Registration Statement.

Debenture Holders will receive a 3-year warrant to purchase shares of the company's stock at $2.00 per share. Debenture Holders will receive this warrant regardless if they convert or not.

Please call with any questions-

Truly,

Francis V. Lorenzo
Vice President - Investment Banking
Charles Vista, LLC.
100 William Street
18th Floor, Suite 1820
New York, NY 10038
Direct: 646.422.3113
Toll Free: 800.799.9070
Main: 212.690.6000
Fax: 212.690.6000
...@charlesvista.com

Div. Ex. 34 (emphasis added). While Frank Lorenzo knew the truth about W2E's parlous financial condition, the emails contained extensive false information, including regarding the company's "three layers of protection." Tr. 269, 283-90, 324-25. Frank Lorenzo does not take personal responsibility for having sent false information to potential investors. Rather, he blames both Gregg Lorenzo for having asked him to send the emails, Tr. 261; Div. Ex. 132 at 141, and W2E, for (as Frank Lorenzo contends) having not sufficiently brought the information about the asset

write-off to his attention, Tr. 231, 246-48, 365. Rothe never invested in the debentures,[9] but Goolcharan did, in the amount of $15,000. Tr. 93-94, 177-78, 260; Div. Ex. 54. Lorenzo earned $150 on Goolcharan's investment. Tr. 412.

Frank Lorenzo sent the emails without even thinking about the contents: "I just didn't give it much thought at the time. My boss asked me to send these e-mails out and I sent them out." Tr. 347. "The guy owns the firm. He just asked me to send out an e-mail for him. I am going to tell him no?" Tr. 382. "I didn't really think about it one way or another. Unfortunately, I hit the send button and it's caused me a lot of grief." Tr. 366. The emails were "erased from my memory two seconds after I sent [them]." Id. Frank Lorenzo characterized his actions as a "mistake" numerous times in his testimony. Tr. 260, 264, 269, 294, 298, 365-67, 370-73.

D. Ability to Pay

At the hearing and in his Proposed Findings of Fact and Conclusions of Law, Frank Lorenzo suggested that he is somewhat impecunious. Tr. 297-98, 354, 385, 401; Resp. Br. at 1 n.1, 6-7. However, he has not otherwise affirmatively asserted an inability to pay a civil money penalty. Nor has he introduced evidence such as financial statements to support such an assertion. Accordingly, Frank Lorenzo has not demonstrated an inability to pay any penalty that may be ordered in this proceeding.

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[9] Rothe, however, read Frank Lorenzo's email. Tr. 177-78.

III. CONCLUSIONS OF LAW

The OIP charges that Frank Lorenzo willfully violated Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. As discussed below, it is concluded that he willfully violated those provisions.

A. Antifraud Provisions

Frank Lorenzo is charged with willfully violating the antifraud provisions of the Securities and Exchange Acts – Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder – which prohibit essentially the same type of conduct. United States v. Naftalin, 441 U.S. 768, 773 n.4, 778 (1979); SEC v. Pimco Advisors Fund Mgmt. LLC, 341 F. Supp. 2d 454, 469 (S.D.N.Y. 2004).

Section 17(a) of the Securities Act makes it unlawful "in the offer or sale of" securities, by jurisdictional means, to:

> 1) employ any device, scheme, or artifice to defraud;
>
> 2) obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary to make the statement made not misleading; or
>
> 3) engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

Similar proscriptions are contained in Exchange Act Section 10(b) and Rule 10b-5.

Scienter is required to establish violations of Securities Act Section 17(a)(1) and Exchange Act Section 10(b) and Rule 10b-5. Aaron v. SEC, 446 U.S. 680, 690-91, 695-97 (1980); SEC v. Steadman, 967 F.2d 636, 641 & n.3 (D.C. Cir. 1992). It is "a mental state embracing intent to deceive, manipulate, or defraud." Aaron, 446 U.S. at 686 n.5; Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193 & n.12 (1976); SEC v. Steadman, 967 F.2d at 641. Recklessness can satisfy the scienter requirement. See David Disner, 52 S.E.C. 1217, 1222 & n.20 (1997); SEC v. Steadman, 967 F.2d at 641-42; Hollinger v. Titan Capital Corp., 914 F.2d 1564, 1568-69 (9th Cir. 1990). Reckless conduct is "conduct which is 'highly unreasonable' and represents 'an extreme departure from the standards of ordinary care . . . to the extent that the danger was either known to the defendant or so obvious that the defendant must have been aware of it.'" Rolf v. Blyth, Eastman Dillon & Co., Inc., 570 F.2d 38, 47 (2d Cir. 1978) (quoting Sanders v. John Nuveen & Co., 554 F.2d 790, 793 (7th Cir. 1977)).

Scienter is not required to establish a violation of Securities Act Section 17(a)(2) or 17(a)(3); a showing of negligence is adequate. See SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 195 (1963); SEC v. Steadman, 967 F.2d at 643 & n.5; Steadman v. SEC, 603 F.2d 1126, 1132-34 (5th Cir. 1979), aff'd on other grounds, 450 U.S. 91 (1981).

Material misrepresentations and omissions violate Securities Act Section 17(a) and Exchange Act Section 10(b) and Rule 10b-5. The standard of materiality is whether or not a reasonable investor or prospective investor would have considered the information

important in deciding whether or not to invest. See Basic Inc. v. Levinson, 485 U.S. 224, 231-32, 240 (1988); TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438, 449 (1976); SEC v. Steadman, 967 F.2d at 643.

1. Willfulness

In addition to requesting a cease-and-desist order pursuant to Sections 8A of the Securities Act and 21C(a) of the Exchange Act, the Division requests sanctions pursuant to Sections 15(b) and 21B of the Exchange Act. Willful violations by Respondent must be found in order to impose sanctions on them pursuant to those provisions. A finding of willfulness does not require an intent to violate, but merely an intent to do the act which constitutes a violation. See Wonsover v. SEC, 205 F.3d 408, 413-15 (D.C. Cir. 2000); Steadman v. SEC, 603 F.2d at 1135; Arthur Lipper Corp. v. SEC, 547 F.2d 171, 180 (2d Cir. 1976); Tager v. SEC, 344 F.2d 5, 8 (2d Cir. 1965).

2. Selective Prosecution

Frank Lorenzo suggests that charging him and not other Charles Vista staffers constitutes selective prosecution. "Selective prosecution," however, is a term of art. "To establish such a claim, a petitioner must demonstrate that he was unfairly singled out for prosecution based on improper considerations such as race, religion, or the desire to prevent the exercise of a constitutionally protected right." Scott Epstein, Exchange Act Release No. 59328 (Jan. 30, 2009), 95 SEC Docket 13833, 13856; accord Robert Radano, Advisers Act Release No. 2750 (June 30, 2008), 93 SEC Docket 7495, 7510 n.74. No such showing was made here. Rather, the Division's decision to charge Frank

Lorenzo and not to charge other individuals was an exercise of prosecutorial discretion. Robert Radano, 93 SEC Docket at 7510 n.74. (citing Dolphin and Bradbury, Inc., Exchange Act Release No. 54143 (July 13, 2006), 88 SEC Docket 1298, 1318, aff'd, 512 F.3d 634 (D.C. Cir. 2008)).

B. Antifraud Violations

The record shows that Frank Lorenzo violated the antifraud provisions by making material misstatements and omissions in the emails. The falsity of the representations in the emails is staggering. The only possible issue is the degree of Frank Lorenzo's culpability. While denying that he intended to defraud, he admits that he was negligent, which as a threshold shows a violation of Securities Act Sections 17(a)(2) and (3). Further, the evidence shows that he was reckless – although he knew that W2E was in terrible financial shape, he sent the emails without thinking. Had he taken a minute to read the text, he would have realized that it was false and misleading and that W2E was not worth anything near what was being represented to potential investors. Also, he cannot escape liability by claiming that Gregg Lorenzo ordered him to send the emails. The fact that Gregg Lorenzo contributed to the misrepresentation does not relieve Frank Lorenzo from responsibility. See James J. Pasztor, 54 S.E.C. 398, 406-07, 411-13 (1999) (supervisor held liable for registered representative's execution of violative directed trades; supervisor had tried to stop the trading but was overruled by broker-dealer's owner who was friendly with the customer); Charles K. Seavey, 56 S.E.C. 357, 364-65, 368 (2003) (associated person found liable where investment adviser required him to sign

materially misleading letter), aff'd, 111 F. App'x. 911 (9th Cir. 2004).

In sum, it is concluded that Frank Lorenzo willfully violated the antifraud provisions of the Securities and Exchange Acts by his material misrepresentations and omissions concerning W2E in the emails.

IV. SANCTIONS

The Division requests a cease-and-desist order, a third-tier civil money penalty, and an industry bar.[10] As discussed below, Frank Lorenzo will be ordered to cease and desist from violations of Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, ordered to pay a third-tier civil penalty of $15,000, and barred from the securities industry.[11]

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[10] The Division does not seek disgorgement. Div. Br. at 26 n.5.

[11] The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act), which became effective on July 22, 2010, provided collateral bars in each of the several statutes regulating different aspects of the securities industry. Frank Lorenzo's wrongdoing occurred before July 22, 2010. However, the Commission has determined that sanctioning a respondent with a collateral bar for pre-Dodd-Frank wrongdoing is not impermissibly retroactive, but rather provides prospective relief from harm to investors and the markets. John W. Lawton, Advisers Act Release No. 3513 (Dec. 13, 2012), 105 SEC Docket 61722, 61737; see also Alfred Clay Ludlum, III, Advisers Act Release No. 3628 (July 11, 2013), 2013 WL 3479060, at *1, 6; Johnny Clifton, Securities Act Release No. 9417 (July 12, 2013), 2013 WL 3487076, at *1, 13; Tzemach David Netzer Korem, Exchange Act Release No. 70044 (July 26, 2013), 2013 WL 3864511, at *1, 7.

A. Sanction Considerations

In determining sanctions, the Commission considers such factors as:

> the egregiousness of the defendant's actions, the isolated or recurrent nature of the infraction, the degree of scienter involved, the sincerity of the defendant's assurances against future violations, the defendant's recognition of the wrongful nature of his conduct, and the likelihood that the defendant's occupation will present opportunities for future violations.

Steadman, 603 F.2d at 1140 (quoting SEC v. Blatt, 583 F.2d 1325, 1334 n.29 (5th Cir. 1978)). The Commission also considers the age of the violation and the degree of harm to investors and the marketplace resulting from the violation. Marshall E. Melton, 56 S.E.C. 695, 698 (2003). Additionally, the Commission considers the extent to which the sanction will have a deterrent effect. Schield Mgmt. Co., Exchange Act Release No. 53201 (Jan. 31, 2006), 87 SEC Docket 848, 862 & n.46. As the Commission has often emphasized, the public interest determination extends to the public-at-large, the welfare of investors as a class, and standards of conduct in the securities business generally. See Christopher A. Lowry, 55 S.E.C. 1133, 1145 (2002), aff'd, 340 F.3d 501 (8th Cir. 2003); Arthur Lipper Corp., 46 S.E.C. 78, 100 (1975). The amount of a sanction depends on the facts of each case and the value of the sanction in preventing a recurrence. See Berko v. SEC, 316 F.2d 137, 141 (2d Cir. 1963); Leo Glassman, 46 S.E.C. 209, 211-12 (1975).

B. Sanctions

1. Cease and Desist

Securities Act Section 8A and Exchange Act Section 21C(a) authorize the Commission to issue a cease-and-desist order against a person who "is violating, has violated, or is about to violate" any provision of those Acts or rules thereunder. Whether there is a reasonable likelihood of such violations in the future must be considered. KPMG Peat Marwick LLP, 54 S.E.C. 1135, 1185 (2001). Such a showing is "significantly less than that required for an injunction." Id. at 1183-91. In determining whether a cease-and-desist order is appropriate, the Commission considers the Steadman factors quoted above, as well as the recency of the violation, the degree of harm to investors or the marketplace, and the combination of sanctions against the respondent. See WHX Corp. v. SEC, 362 F.3d 854, 859-61 (D.C. Cir. 2004); KPMG, 54 S.E.C. at 1192.

Frank Lorenzo's conduct was egregious and repeated – he sent the violative email to two people. The conduct involved at least a reckless degree of scienter. The lack of assurances against future violations and recognition of the wrongful nature of the conduct goes beyond a vigorous defense of the charges. His attempt to displace blame onto both Gregg Lorenzo and W2E is an aggravating factor. His chosen occupation in the financial industry will present opportunities for future violations. The violations were neither recent nor remote in time, having occurred about four years ago. The evidence of record does not quantify the degree of harm to the marketplace in dollars but harm is evident from the dishonest nature

of Frank Lorenzo's misconduct. In light of these considerations, a cease-and-desist order is appropriate.

Frank Lorenzo's lack of a disciplinary history does not remove the need for sanctions. Mitchell M. Maynard, Advisers Act Release No. 2875 (May 15, 2009), 95 SEC Docket 16844, 6860 & n.39 ("[T]he absence of disciplinary history is not mitigative as securities professionals should not be rewarded for complying with securities laws.").

2. Civil Money Penalty

Section 21B of the Exchange Act authorizes the Commission to impose civil money penalties for willful violations of the Securities and Exchange Acts or rules thereunder. In considering whether a penalty is in the public interest, the Commission may consider six factors: (1) fraud; (2) harm to others; (3) unjust enrichment; (4) previous violations; (5) deterrence; and (6) such other matters as justice may require. See Section 21B(c) of the Exchange Act; New Allied Dev. Corp., 52 S.E.C. 1119, 1130 n.33 (1996); First Sec. Transfer Sys., Inc., 52 S.E.C. 392, 395-96 (1995); see also Jay Houston Meadows, 52 S.E.C. 778, 787-88 (1996), aff'd, 119 F.3d 1219 (5th Cir. 1997); Consol. Inv. Servs., Inc., 52 S.E.C. 582, 590-91 (1996).

As to Frank Lorenzo, there are no mitigating factors. He violated the antifraud provisions, so his violative actions "involved fraud [and] reckless disregard of a regulatory requirement [and] created a significant risk of substantial losses to other persons" within the meaning of Section 21B of the Exchange Act. Deterrence also requires a substantial penalty against him.

Penalties are in the public interest in this case. Penalties in addition to the other sanctions ordered are necessary for the purpose of deterrence. See Section 21B(c)(5) of the Exchange Act; H.R. Rep. No. 101-616, at 17 (1990), reprinted in 1990 U.S.C.C.A.N. 1379, 1384. The Division requests that Frank Lorenzo be ordered to pay third-tier penalties, without specifying dollar amounts or units of violation. In addition to arguing that there were no violations, Respondent argues that civil penalties are not warranted, much less third-tier penalties. A third-tier penalty, as the Division requests, is appropriate because Frank Lorenzo's violative acts involved fraud and resulted in the risk of substantial losses to other persons. See Section 21B(b)(3) of the Exchange Act. Under that provision, for each violative act or omission during the time at issue the maximum third-tier penalty is $150,000 for a natural person. 17 C.F.R. § 201.1004. The provision, like most civil penalty statutes, leaves the precise unit of violation undefined. See Colin S. Diver, The Assessment and Mitigation of Civil Money Penalties by Federal Administrative Agencies, 79 Colum. L. Rev. 1435, 1440-41 (1979).

The events at issue will be considered as one course of action, and a third-tier penalty amount of $15,000 will be ordered against Frank Lorenzo. Combined with the other sanctions ordered, a third-tier penalty of $15,000 – less than the maximum and equivalent to the actual loss sustained by investor Goolcharan – is in the public interest.

3. Bar

The Division requests that Frank Lorenzo be barred from the securities industry. Combined with other

sanctions ordered, bars are in the public interest and appropriate deterrents. The violations involved scienter. Frank Lorenzo's business provides him with the opportunity to commit violations of the securities laws in the future. The record shows a lack of recognition of the wrongful nature of the violative conduct. His attempts to deflect blame onto others are aggravating factors. In short, it is necessary in the public interest and for the protection of investors that Frank Lorenzo be barred from the industry.

V. RECORD CERTIFICATION

Pursuant to Rule 351(b) of the Commission's Rules of Practice, 17 C.F.R. § 201.351(b), it is certified that the record includes the items set forth in the record index issued by the Secretary of the Commission on November 26, 2013, plus Frank Lorenzo's Proposed Findings of Fact and Conclusions of Law, dated November 14, 2013.

VI. ORDER

IT IS ORDERED that, pursuant to Sections 8A of the Securities Act and 21C(a) of the Exchange Act, FRANCIS V. LORENZO CEASE AND DESIST from committing or causing any violations or future violations of Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

IT IS FURTHER ORDERED that, pursuant to Section 21B of the Exchange Act, FRANCIS V. LORENZO PAY A CIVIL MONEY PENALTY of $15,000.

IT IS FURTHER ORDERED that, pursuant to Section 15(b) of the Exchange Act, FRANCIS V. LORENZO IS BARRED from associating with any broker, dealer, investment adviser, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization and from participating in an offering of penny stock.[12]

Payment of penalties shall be made on the first day following the day this Initial Decision becomes final. Payment shall be made by certified check, United States postal money order, bank cashier's check, wire transfer, or bank money order, payable to the Securities and Exchange Commission. See 17 C.F.R. § 201.601(a), (c). The payment, and a cover letter identifying the Respondent and Administrative Proceeding No. 3-15211, shall be delivered to: Enterprises Services Center, Accounts Receivable Branch, HQ Bldg., Room 181, AMZ-341, 6500 South MacArthur Blvd., Oklahoma City, Oklahoma 73169. A copy of the cover letter and instrument of payment shall be sent to the Commission's Division of Enforcement, directed to the attention of counsel of record.

This Initial Decision shall become effective in accordance with and subject to the provisions of Rule 360 of the Commission's Rules of Practice, 17 C.F.R.

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[12] Thus, he will be barred from acting as a promoter, finder, consultant, or agent; or otherwise engaging in activities with a broker, dealer, or issuer for purposes of the issuance or trading in any penny stock, or inducing or attempting to induce the purchase or sale of any penny stock, pursuant to Exchange Act Section 15(b)(6)(A), (C).

§ 201.360. Pursuant to that Rule, a party may file a petition for review of this Initial Decision within twenty-one days after service of the Initial Decision. A party may also file a motion to correct a manifest error of fact within ten days of the Initial Decision, pursuant to Rule 111(h) of the Commission's Rules of Practice, 17 C.F.R. § 201.111(h). If a motion to correct a manifest error of fact is filed by a party, then that party shall have twenty-one days to file a petition for review from the date of the undersigned's order resolving such motion to correct a manifest error of fact. The Initial Decision will not become final until the Commission enters an order of finality. The Commission will enter an order of finality unless a party files a petition for review or a motion to correct a manifest error of fact or the Commission determines on its own initiative to review the Initial Decision as to a party. If any of these events occur, the Initial Decision shall not become final as to that party.

Carol Fox Foelak
Administrative Law Judge

No. 17-1077

In the Supreme Court of the United States

FRANCIS V. LORENZO, PETITIONER

v.

SECURITIES AND EXCHANGE COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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QUESTION PRESENTED

Whether, in an enforcement proceeding brought by the Securities and Exchange Commission, a person who knowingly disseminates false or misleading statements in connection with a securities transaction can be found to have violated Section 17(a)(1) of the Securities Act of 1933, 15 U.S.C. 77q(a)(1) (2006); Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. 78j(b) (2006); and Rule 10b-5(a) and (c), 17 C.F.R. 240.10b-5(a) and (c), even if the person does not "make" false or misleading statements for purposes of Rule 10b-5(b), 17 C.F.R. 240.10b-5(b).

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In the Supreme Court of the United States

No. 17-1077

FRANCIS V. LORENZO, PETITIONER

v.

SECURITIES AND EXCHANGE COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1-50) is reported at 872 F.3d 578. The opinion and order of the Securities and Exchange Commission (Pet. App. 51-95, 96-97) are reported at 111 SEC Docket 1761 and are available at 2015 WL 1927763. The initial decision of the administrative law judge (Pet. App. 98-121) is reported at 107 SEC Docket 5934 and is available at 2013 WL 6858820.

JURISDICTION

The judgment of the court of appeals was entered on September 29, 2017. On December 19, 2017, the Chief Justice extended the time within which to file a petition for a writ of certiorari to and including January 26, 2018, and the petition was filed on that date. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

Petitioner, an investment banker, sent two emails containing false statements to prospective investors. Pet. App. 3-5. The Securities and Exchange Commission (SEC or Commission) initiated administrative proceedings and determined that petitioner had violated Section 17(a)(1) of the Securities Act of 1933, 15 U.S.C. 77q(a)(1) (2006); Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. 78j(b) (2006); and SEC Rule 10b-5, 17 C.F.R. 240.10b-5. Pet. App. 5-6.[1] The Commission imposed a cease-and-desist order, a civil penalty, and a lifetime bar from the securities industry. *Id.* at 6. On petition for review, the court of appeals held that petitioner had not violated Rule 10b-5(b) but that he had violated Section 17(a)(1), Section 10(b), and Rule 10b-5(a) and (c). *Id.* at 14-34. The court vacated the civil penalty and industry bar and remanded to the Commission, where proceedings are ongoing. *Id.* at 35-37.

1. Petitioner worked as the director of investment banking at Charles Vista, LLC, a registered broker-dealer that petitioner described as "'a small boiler room'" where representatives "engaged in high-pressure sales tactics" and "seemed to be 'stretching the truth.'" Pet. App. 53-54. During the relevant period, petitioner's only client was Waste2Energy Holdings, Inc. (W2E), a start-up seeking to develop a "gasification" technology that could generate electricity from solid waste. *Id.* at 3. W2E's technology "never materialized," and the company "sought to escape financial ruin" by offering up to $15 million in convertible debentures—debt secured by the company's potential future earning power rather

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[1] All citations to the securities laws in the context of petitioner's case refer to the statutes in force at the time of his relevant conduct.

than by its existing assets. *Ibid.* Charles Vista served as the placement agent for W2E's debenture offering. *Id.* at 3-4.

Petitioner knew that W2E's technology "didn't really work" and that the company's financial condition "was horrible." Pet. App. 55. On October 1, 2009, W2E submitted SEC filings stating that its gasification technology and related assets that it had previously valued at more than $10 million had "no value," and that its total assets amounted to $660,408. *Id.* at 4 (citation omitted). Petitioner was aware of the filings and received an email explaining the write-off from W2E's chief financial officer. *Id.* at 4-5.

Petitioner nevertheless continued to seek investors for W2E's debenture offering. On October 14, 2009, petitioner sent two emails to prospective investors, with the subject "W2E Debenture Deal Points." Pet. App. 5, 59. The text of the emails, which petitioner contends was supplied by Charles Vista owner Gregg Lorenzo,[2] stated that the W2E debenture offering came with "3 layers of protection: (I) [W2E] has over $10 mm in confirmed assets; (II) [W2E] has purchase orders and" letters of intent "for over $43 mm in orders; (III) Charles Vista has agreed to raise additional monies to repay these Debenture holders (if necessary)." *Id.* at 5, 16-18 (citation omitted; brackets in original). One email stated that petitioner had sent it "[a]t the request of Gregg Lorenzo." *Id.* at 5 (citation omitted; brackets in original). The other email stated that it had been sent "[a]t the request of" a Charles Vista broker and Gregg Lorenzo. *Ibid.* (citation omitted; brackets in original). Petitioner signed both messages with his name and title as "Vice President—

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[2] Gregg Lorenzo is not related to petitioner. See Pet. App. 3.

Investment Banking," and he told potential investors to contact him if they had any questions. *Ibid.*; see *id.* at 107-108 (reproducing full text of email). Petitioner later admitted that he "knew" that each of the critical statements in the two emails "was false and/or misleading when he sent them." *Id.* at 53.

2. a. The SEC instituted administrative proceedings against petitioner and charged him with violating three securities-fraud provisions. See Pet. App. 5.

First, the Commission charged petitioner with violating Section 17(a)(1). In relevant part, that provision makes it "unlawful for any person in the offer or sale of any securities * * * to employ any device, scheme, or artifice to defraud." 15 U.S.C. 77q(a)(1).

Second, the Commission charged petitioner with violating Section 10(b). In relevant part, Section 10(b) makes it "unlawful for any person * * * [t]o use or employ, in connection with the purchase or sale of any security * * * [,] any manipulative or deceptive device or contrivance in contravention of" the Commission's "rules and regulations." 15 U.S.C. 78j(b).

Third, the Commission charged petitioner with violating Rule 10b-5. In relevant part, that Rule makes it unlawful:

> (a) To employ any device, scheme, or artifice to defraud,
>
> (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (c) To engage in any act, practice, or course of business which operates or would operate as a

> fraud or deceit upon any person, in connection with the purchase or sale of any security.

17 C.F.R. 240.10b-5.[3]

b. Petitioner contested the charges before an administrative law judge (ALJ). After a hearing, the ALJ found that petitioner "knew the truth about W2E's parlous financial condition" when he sent the two emails, which contained representations "staggering" in their "falsity." Pet. App. 108, 113. The ALJ concluded that petitioner had "willfully" violated each of the charged provisions "by his material misrepresentations and omissions concerning W2E in the emails." *Id.* at 114.

c. Petitioner sought review before the Commission, which conducted "an independent review of the record" and found that petitioner had violated each of the charged provisions. Pet. App. 53. Specifically, the SEC determined that petitioner had violated subsection (b) of Rule 10b-5 by making materially misleading statements in the two emails sent to prospective investors. *Id.* at 76; see *id.* at 73-76. The SEC separately determined that petitioner had violated Section 17(a)(1), Section 10(b), and subsections (a) and (c) of Rule 10b-5 by knowingly sending "materially misleading language from his own email account to prospective investors." *Id.* at 77. The Commission explained that petitioner's "role in producing and sending the emails constituted employing a deceptive 'device,' 'act,' or 'artifice to defraud' for purposes of liability under" those provisions, "[i]ndependently of whether" petitioner's "involvement in the

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[3] The SEC brought the same charges against Gregg Lorenzo and Charles Vista. Both those parties settled with the Commission. Pet. App. 5-6.

emails amounted to 'making' the misstatements for purposes of Rule 10b-5(b)." *Id.* at 77. As sanctions, the Commission imposed a cease-and-desist order, a $15,000 civil penalty, and a lifetime bar from the securities industry. *Id.* at 79.

3. Petitioner filed a petition for review in the court of appeals, challenging the Commission's liability determination and its imposition of an industry-wide bar and a $15,000 civil penalty. Pet. App. 7. The court granted the petition in part, vacated the challenged sanctions, and remanded for further proceedings. *Id.* at 36-37.

The court of appeals first held that substantial evidence supported the Commission's determination that the statements in the emails were false or misleading and that petitioner had acted with the requisite scienter. Pet. App. 7-14. Petitioner does not seek this Court's review of those aspects of the decision.

The court of appeals next held that petitioner had not violated Rule 10b-5(b) because he did not "make" the misleading statements in the emails. Pet. App. 15. Rather, the court concluded, the "maker" of those statements was petitioner's boss, Gregg Lorenzo. *Id.* at 16. The court relied on *Janus Capital Group, Inc.* v. *First Derivative Traders*, 564 U.S. 135 (2011), in which this Court held that a person "make[s]" a statement under Rule 10b-5(b) only if he has "ultimate authority over the statement, including its content and whether and how to communicate it." *Id.* at 142. The court of appeals concluded that Gregg Lorenzo had "ultimate authority" over the statements in the emails, and that he was therefore "the maker" of the statements for purposes of Rule 10b-5(b). Pet. App. 19 (citation omitted).

The court of appeals further held, however, that petitioner had violated Section 17(a)(1), Section 10(b), and

Rule 10b-5(a) and (c). Pet. App. 20-22. The court explained that those provisions, unlike Rule 10b-5(b), do not require that a violator "make" a false statement. *Id.* at 20. Rather, those provisions prohibit employing a fraudulent "device," "practice," or "scheme." *Id.* at 20-21 (citations omitted). The court found that petitioner's conduct in producing and sending emails containing false statements "fits comfortably within the ordinary understanding of" of the text of those prohibitions. *Id.* at 21. The court further observed that petitioner had presented "no argument that his actions fail to satisfy the statutory and regulatory language," and that he had not challenged the SEC's rejection of his "suggestion that he merely passed along the messages in his own name without thinking about their content." *Id.* at 22.

The court of appeals declined "to reach the merits" of petitioner's challenge to the sanctions. Pet. App. 35. Because the court had "no assurance that the Commission would have imposed the same level of penalties in the absence of its finding of liability for making false statements under Rule 10b-5(b)," the court vacated the sanctions that the SEC had previously imposed, and it remanded to the agency for further proceedings. *Ibid.*

Judge Kavanaugh dissented. As relevant here, he disagreed with the majority that petitioner had violated Section 17(a)(1), Section 10(b), and Rule 10b-5(a) and (c). Pet. App. 46. In his view, liability under those provisions "must be based on conduct that goes beyond a defendant's role in preparing mere misstatements or omissions made by others." *Ibid.* He would have vacated the Commission's order with respect to both liability and sanctions. *Id.* at 37-38, 46.

4. The remand proceedings before the Commission are currently ongoing. *Inter alia*, the SEC has ordered

the parties to brief "what sanctions, if any, are appropriate." *In re Lorenzo*, Securities Act Release No. 3-15211, 2017 WL 6349871, at *1 (Dec. 12, 2017).

ARGUMENT

Petitioner challenges (Pet. 23-32) the court of appeals' determination that he violated Section 17(a)(1), Section 10(b), and Rule 10b-5(a) and (c). The court correctly held that those provisions encompass petitioner's dissemination of false or misleading statements to prospective investors. Petitioner also contends (Pet. 13-23) that the courts of appeals are divided over whether conduct like his is actionable under the securities laws. But petitioner does not identify any conflict over the scope of liability under Section 17(a)(1). With respect to Section 10(b) and Rule 10b-5(a) and (c), the decisions that petitioner views as inconsistent with the decision below have involved different conduct by the defendants, and they arose out of suits brought by private plaintiffs, rather than (as in this case) an administrative enforcement action brought by the SEC. The current interlocutory posture of the case, and the pendency before the Commission of proceedings in which petitioner is actively challenging the sanctions that the agency previously imposed, provide a further reason to deny review.

1. The court of appeals correctly held that petitioner's misconduct violated Section 17(a)(1), Section 10(b), and Rule 10b-5(a) and (c). Pet. App. 19-34.

a. The "statutory text controls the definition of conduct covered by" the federal securities laws. *Central Bank of Denver, N.A.* v. *First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 175 (1994); see *Morrison* v. *National Australia Bank Ltd.*, 561 U.S. 247, 261 n.5 (2010). As relevant here, Section 17(a)(1) makes it unlawful "to

employ any device, scheme, or artifice to defraud" in offering or selling a security. 15 U.S.C. 77q(a)(1). Rule 10b-5(a), incorporated through Section 10(b), prohibits "employ[ing] any device, scheme, or artifice to defraud * * * in connection with the purchase or sale of any security." 17 C.F.R. 240.10b-5(a). Rule 10b-5(c), also incorporated through Section 10(b), bars "engag[ing] in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person * * * in connection with the purchase or sale of any security." 17 C.F.R. 240.10b-5(c).

Petitioner's conduct "fits comfortably within the ordinary understanding of" those statutory and regulatory prohibitions. Pet. App. 20. "Words and phrases like 'fraud,' 'deceit,' and 'device, scheme or artifice' provide a broad linguistic frame within which a large number of practices may fit." *SEC* v. *Clark*, 915 F.2d 439, 448 (9th Cir. 1990); see *Aaron* v. *SEC*, 446 U.S. 680, 696 n.13 (1980) (citing dictionary definitions); *Affiliated Ute Citizens* v. *United States*, 406 U.S. 128, 151 (1972) (stating that the "proscriptions" in Section 10(b) and Rule 10b-5 "are broad and, by repeated use of the word 'any,' are obviously meant to be inclusive"). Knowingly sending "email messages containing false statements" about a company's financial prospects "directly to potential investors," in order to induce recipients to participate in a debenture offering, is naturally described as employing a device, scheme, artifice, or act to defraud. Pet. App. 20; see, *e.g.*, *United States* v. *Williams*, 865 F.3d 1302, 1309 (10th Cir.) ("[S]cheme and artifice are defined to include . . . fraudulent pretenses or misrepresentations intended to deceive others to obtain something of value, such as money.") (citation omitted; brackets in original), cert. denied, 138 S. Ct. 567 (2017).

Indeed, petitioner "presents no argument that his actions fail to satisfy the statutory and regulatory language. He does not examine—or even reference—the text of those provisions in arguing that they should be deemed not to apply to his conduct." Pet. App. 22. The "text of the statute" accordingly "controls [the] decision" here. *Central Bank of Denver*, 511 U.S. at 173.

The history and purpose of the relevant provisions reinforce the conclusion that they encompass petitioner's conduct. Congress enacted the federal securities laws to "insure honest securities markets and thereby promote investor confidence," and to "achieve a high standard of business ethics in the securities industry." *SEC* v. *Zandford*, 535 U.S. 813, 819 (2002) (citations and internal quotation marks omitted); see *SEC* v. *Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 198 (1963). The antifraud provisions of the Securities Act and the Exchange Act therefore must be "construed not technically and restrictively, but flexibly to effectuate [their] remedial purposes." *Zandford*, 535 U.S. at 819 (citations and internal quotation marks omitted); see, *e.g.*, *Santa Fe Indus., Inc.* v. *Green*, 430 U.S. 462, 475-476 (1977); *Capital Gains*, 375 U.S. at 186. Petitioner's dissemination of false statements to prospective investors, in hopes of attracting support for W2E's debenture offering, directly implicates Congress's market-protective purposes. Pet. App. 22.

2. a. Petitioner contends (Pet. 24-26) that fraud claims involving false statements can proceed only under Section 17(a)(2) and Rule 10b-5(b). As relevant here, those provisions make it unlawful "to obtain money or property by means of any untrue statement of a material fact," 15 U.S.C. 77q(a)(2), or "[t]o make any untrue statement of a material fact," 17 C.F.R. 240.10b-5(b), in

connection with a securities transaction. But nothing in the text, structure, history, or purpose of the relevant provisions suggests that the references to "statement[s]" in Section 17(a)(2) and Rule 10b-5(b) mean that a fraud claim based on false statements can proceed *only* under those two provisions.

The fact that a person can be liable for *making* a false statement under Rule 10b-5(b) does not preclude the imposition of liability for *disseminating* a false statement as part of a "device, scheme, or artifice to defraud" under Section 17(a)(1) or Rule 10b-5(a), or as part of an "act, practice, or course of business which operates * * * as a fraud" under Rule 10b-5(c). 17 C.F.R. 240.10b-5(a) and (c). To the contrary, "[e]ach succeeding prohibition" of Section 17(a) "is meant to cover additional kinds of illegalities—not to narrow the reach of the prior sections." *United States* v. *Naftalin*, 441 U.S. 768, 774 (1979). Similarly, while Rule 10b-5(b) "specifies the making of an untrue statement," the "first and third subparagraphs are not so restricted." *Affiliated Ute*, 406 U.S. at 153; see *Chadbourne & Parke LLP* v. *Troice*, 134 S. Ct. 1058, 1063 (2014) (noting that Rule 10b-5 covers fraudulent conduct beyond "the making of" false statements). Indeed, "[i]t would be arbitrary to read th[e] terms" of Section 17(a)(1) and Rule 10b-5(a) and (c) "as *excluding* the making, drafting, or devising of a misstatement or omission." *In re Dennis J. Malouf*, Securities Act Release No. 4463, 2016 WL 4035575, at *8 (July 27, 2016), petition for rev. filed, *Malouf* v. *SEC*, No. 16-9546 (10th Cir. Sept. 8, 2016). The court of appeals correctly declined "to treat the various provisions as occupying mutually exclusive territory, such that false-statement cases must reside exclusively within the province of Rule 10b-5(b)." Pet. App. 26.

The history of the relevant provisions confirms that Congress and the Commission did not confine all false-statement claims to Section 17(a)(2) and Rule 10b-5(b). It is "hardly a novel proposition" that different provisions of the securities laws "'prohibit some of the same conduct.'" *Herman & MacLean* v. *Huddleston*, 459 U.S. 375, 383 (1983) (citation omitted). "The Securities Act of 1933 was the first experiment in federal regulation of the securities industry," and it was "understandable" that Section 17(a) "include[d] both a general proscription against fraudulent and deceptive practices and, out of an abundance of caution, a specific proscription against" nondisclosure under Section 17(a)(2), even though "a specific proscription against nondisclosure" was arguably "surplusage." *Capital Gains*, 375 U.S. at 197-199. Rule 10b-5 likewise reflects the SEC's intent to stamp out fraud in the purchase or sale of securities. See *Conference on Codification of the Federal Securities Laws*, 22 Bus. Law. 793, 922 (1967). The Commission accordingly based Rule 10b-5 on Section 17(a), and it has long interpreted the subsections of the two provisions as "mutually supporting rather than mutually exclusive." *In re Cady, Roberts & Co.*, 40 S.E.C. 907, 1961 WL 60638, at *4 (Nov. 8, 1961).

Indeed, in its early years, the Commission did not explicitly distinguish between subsections in finding violations of Rule 10b-5. See, *e.g.*, *In re Ward La France Truck Corp.*, 13 S.E.C. 373, 1943 WL 29807 (May 20, 1943). The presence of "some overlap" among the anti-fraud provisions therefore "is neither unusual nor unfortunate." *SEC* v. *National Sec., Inc.*, 393 U.S. 453, 468 (1969). Rather, it reflects that those provisions are to "be read flexibly, not technically or restrictively." *Zandford*, 535 U.S. at 821 (citation omitted).

b. Petitioner contends (Pet. 25-30) that the decision below is inconsistent with this Court's decision in *Janus Capital Group, Inc.* v. *First Derivative Traders*, 564 U.S. 135 (2011). That argument lacks merit.

In *Janus*, this Court addressed whether a mutual-fund investment adviser could be held liable in a private action under Rule 10b-5(b) for "mak[ing]" materially false statements in its client mutual funds' prospectuses. 564 U.S. at 137 (quoting 17 C.F.R. 240.10b-5(b)) (brackets in original). The Court concluded that the adviser could not be held liable under that provision because it did not "make" the statements in the prospectuses, as subsection (b) requires. *Id.* at 146. "For purposes of Rule 10b-5," the Court explained, "the maker of a statement is the person or entity with ultimate authority over the statement, including its content and whether and how to communicate it." *Id.* at 142. Because only the mutual fund itself had authority over the statements in the prospectuses, only the fund could be liable under Rule 10b-5(b) for "mak[ing]" false statements. *Id.* at 146.

Applying *Janus*, the court below held that petitioner was not liable under Rule 10b-5(b) for "mak[ing]" false statements because only his boss, Gregg Lorenzo, had "ultimate authority" over the statements in the emails. Pet. App. 19 (quoting *Janus*, 564 U.S. at 142). But as the court of appeals explained, a non-maker of a statement can be liable under Section 17(a), Section 10(b), and subsections (a) and (c) of Rule 10b-5 if he carries out a device, scheme, artifice, or act to defraud. See *id.* at 20. That conclusion is compelled by the text, structure, history, and purpose of those provisions, and it is fully consistent with *Janus*, which did not address the scope of liability under any provision other than Rule 10b-5(b). The *Janus* Court did not suggest that an individual's

failure to "make" a misstatement for purposes of subsection (b) precludes liability under the other antifraud provisions for deceptive conduct that involves disseminating misstatements. See *U.S. SEC* v. *Big Apple Consulting USA, Inc.*, 783 F.3d 786, 797 (11th Cir. 2015) (stating that, because *Janus*'s reasoning is based on the text of Rule 10b-5(b), its holding "does not apply" beyond that subsection) (citation omitted); *SEC* v. *Monterosso*, 756 F.3d 1326, 1334 (11th Cir. 2014) (per curiam) ("*Janus* only discussed what it means to 'make' a statement for purposes of Rule 10b-5(b), and did not concern * * * Rule 10b-5(a) or (c)."); *SEC* v. *Pentagon Capital Mgmt. PLC*, 725 F.3d 279, 287 (2d Cir. 2013) ("[S]ubsection (b) * * * was the only subsection at issue in *Janus*.").

Nor does the decision below "erase[ ] the distinction between primary and secondary liability" (Pet. 25) that this Court emphasized in *Janus* and *Central Bank of Denver*. In *Central Bank of Denver*, the Court explained that defendants in a private suit under Rule 10b-5 may be held liable only if they personally engage in the prohibited conduct. 511 U.S. at 177. Merely "giving aid to a person who commits" a prohibited act does not suffice. *Ibid.*; see *Janus*, 564 U.S. at 143 ("Rule 10b-5's private right of action does not include suits against aiders and abettors."). But petitioner was not found secondarily liable for aiding and abetting his boss's making of a false statement under Rule 10b-5(b). He was found primarily liable for his "active 'role in producing and sending'" misstatements with an intent to deceive, and for thereby "'employing a deceptive 'device,' 'act,' or 'artifice to defraud' for purposes of liability under Section 10(b), Rule 10b-5(a) and (c), and Section 17(a)(1).'" Pet. App. 21 (citation omitted).

Petitioner attempts to characterize his conduct as aiding and abetting by asserting (Pet. 30) that his "actions in sending emails to two investors were only ministerial," and that he (Pet. 31) simply "facilitat[ed] * * * the distribution of misstatements that were made by others." But petitioner did not simply assist in Gregg Lorenzo's transmittal of misinformation. Rather, petitioner "effectively vouched for the emails' content and put his reputation on the line by listing his personal phone number and inviting the recipients to 'call with any questions.'" Pet. App. 24; see *id.* at 34 (explaining that petitioner "sent the statements to potential investors carrying his stamp of approval as investment banking director"). Imposition of liability under these circumstances is fully consistent with *Janus*. Whereas the mutual-fund advisers in *Janus* likely would not be liable under the principles applied here because those advisers played no active role in disseminating the misstatements, petitioner both transmitted and effectively endorsed Gregg Lorenzo's misrepresentations. See *id.* at 24; accord *Stoneridge Inv. Partners, LLC* v. *Scientific-Atl., Inc.*, 552 U.S. 148, 155 (2008) (noting that defendants determined not to be primarily liable under Rule 10b-5(b) "had no role" in "disseminating" the misstatements in question).[4]

Petitioner also invokes (Pet. 9-12) the assertion of the dissenting judge below, premised on the factual findings of the ALJ, that petitioner lacked the scienter needed for liability under the relevant provisions because he drafted and sent the emails without thinking about their contents. See Pet. App. 39-40 (Kavanaugh, J., dissenting).

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[4] Unlike a private plaintiff, the SEC can bring an action based on aiding-and-abetting liability. See 15 U.S.C. 78t(e); *Janus*, 564 U.S. at 143. The SEC, however, did not pursue such a theory here.

As the court of appeals explained, however, petitioner *disavowed* that view of his own mental state in his brief to the court below, arguing instead that he lacked the requisite scienter because he believed the statements in the emails to be true. See *id.* at 22, 28. And the record amply supports the SEC's determination that petitioner knew the statements in the emails to be false. "One of [petitioner's] chief duties involved conducting due diligence on his clients, including reviewing their financial statements and public SEC filings." *Id.* at 9. Petitioner "knew that W2E's financial situation was 'horrible from the beginning' and that its gas-conversion technology had not worked as planned." *Ibid.* (citation omitted). But petitioner, "having taken stock of the emails' content and having formed the requisite intent to deceive, conveyed materially false information to prospective investors about a pending securities offering backed by the weight of his office as director of investment banking." *Id.* at 22. In any event, a fact-specific dispute about the adequacy of the mental-state evidence in this case would not present any question of general importance warranting this Court's review.

Petitioner suggests (Pet. 26) that the decision below will open the door to private suits against "large numbers of defendants who would otherwise be secondary actors and immune from suit by private plaintiffs because they did not make the misstatements at issue." That concern is misplaced. As explained above, defendants similarly situated to those in *Janus* and *Stoneridge* likely would not be liable under the decision in this case. Unlike the Commission, moreover, private plaintiffs must show reliance on the defendant's misconduct, see *SEC* v. *Morgan Keegan & Co.*, 678 F.3d 1233, 1244 (11th Cir. 2012) (per curiam) (collecting authorities), as well

as economic loss and loss causation, see *Dura Pharms., Inc.* v. *Broudo*, 544 U.S. 336, 341-342 (2005). And if a private plaintiff asserts a Rule 10b-5(a) or (c) claim involving misrepresentations or omissions, the defendant may argue that the heightened pleading standards set forth in the Private Securities Litigation Reform Act of 1995 (PSLRA), Pub. L. No. 104-67, 109 Stat. 737, apply to those allegations. See 15 U.S.C. 78u-4(b)(1). Petitioner's concern that the decision below will encourage meritless private suits is accordingly unwarranted.

3. Petitioner contends (Pet. 13-23) that this Court's review is warranted to resolve a conflict among the courts of appeals. That argument lacks merit. Petitioner identifies no sound reason to believe that any other circuit would have reached a different result under the circumstances presented here.

The absence of a circuit conflict is particularly clear with respect to the D.C. Circuit's application of Section 17(a). No court of appeals has rejected the proposition that liability under Section 17(a)(1) may be premised on a defendant's dissemination of false statements. Pet. App. 25-26. And no court of appeals has read *Janus* to require that a defendant must "make" a false statement in order to be held liable under Section 17(a). The only other circuit that has considered the question has concluded that *Janus* has no bearing on the proper interpretation of Section 17(a). See *Big Apple Consulting*, 783 F.3d at 798 (stating that Section 17(a)(1) and (a)(3) "are in no way directly or indirectly affected by the *Janus* decision"); *Monterosso*, 756 F.3d at 1334.

With respect to Section 10(b) and Rule 10b-5(a) and (c), none of the decisions that petitioner identifies as forming a "majority" position (Pet. 17-21) involved the kind of conduct at issue here—knowing dissemination of a

false statement directly to investors with intent to induce a financial transaction. And all the cases that petitioner cites were initiated by private plaintiffs rather than by the Commission. That distinction is significant because different statutory and other standards govern private securities-fraud actions. See, *e.g.*, *Troice*, 134 S. Ct. at 1063 ("The scope of the private right of action [under Rule 10b-5] is more limited than the scope of the statutes upon which it is based.").

Of particular relevance here, the PSLRA—which does not apply to actions brought by the Commission—requires that, "if an allegation regarding the *statement or omission* is made on information and belief, the complaint shall state with particularity all facts on which that belief is formed." 15 U.S.C. 78u-4(b)(1) (emphasis added). Some courts have read the reference to a "statement or omission" in the PSLRA to indicate that the heightened pleading requirement applies only to Rule 10b-5(b), which expressly refers to statements or omissions. See, *e.g.*, *In re Alstom SA Sec. Litig.*, 406 F. Supp. 2d 433, 474 (S.D.N.Y. 2005). Some courts have then interpreted Rule 10b-5(a) and (c) to exclude all claims involving false statements or omissions, on the theory that a contrary reading would enable private litigants to evade the PSLRA.

The Second Circuit, for example, has stated that, "where the sole basis for such claims is alleged misrepresentations or omissions, plaintiffs have not made out a market manipulation claim under Rule 10b-5(a) and (c), *and remain subject to the heightened pleading requirements of the PSLRA.*" *Lentell* v. *Merrill Lynch & Co.*, 396 F.3d 161, 177 (emphasis added), cert. denied, 546 U.S. 935 (2005). The Eighth Circuit has similarly assumed that the PSLRA's heightened pleading requirements do

not apply to claims under Rule 10b-5(a) and (c), and it has concluded that "misrepresentation claims under Rule 10b-5(b) cannot simply be recast as scheme liability claims under Rules 10b-5(a) and (c)." *Public Pension Fund Grp.* v. *KV Pharm. Co.*, 679 F.3d 972, 986 (2012). The Ninth Circuit, citing *Lentell*, has concluded that "a Rule 10b-5(b) omissions claim" may not be "recast as Rule 10b-5(a) or (c) scheme liability claim." *WPP Luxembourg Gamma Three Sarl* v. *Spot Runner, Inc.*, 655 F.3d 1039, 1057 (2011).

The plain text of the PSLRA encompasses any "statement or omission" that is alleged to have played a role in a violation of the securities laws. The statutory text does not distinguish between statements or omissions that are fraudulent under Rule 10b-5(b) and statements or omissions that constitute (or are used to carry out) a deceptive device, act, or artifice to defraud under Rule 10b-5(a) or (c). 15 U.S.C. 78u-4(b)(1). There is accordingly no need to exclude false-statement claims from Rule 10b-5(a) and (c) in order to prevent evasion of the PSLRA.

The decisions cited by petitioner, moreover, rest on a concern that is wholly absent here, because the PSLRA does not apply to cases initiated by the Commission. There is accordingly no reason to believe that any other circuit would reach a result different from the court below in an SEC enforcement proceeding. See Pet. App. 33. Indeed, the only other court of appeals that has addressed the question presented in a case to which the Commission was a party has reached the same conclusion as the court below. See *Big Apple Consulting*, 783 F.3d at 795-796; *Monterosso*, 756 F.3d at 1334.[5]

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[5] Petitioner's reliance (Pet. 18) on *Desai* v. *Deutsche Bank Securities Ltd.*, 573 F.3d 931 (9th Cir. 2009) (per curiam), is particularly

4. Finally, the interlocutory posture of this case "alone furnishe[s] sufficient ground for the denial" of the petition. *Hamilton-Brown Shoe Co.* v. *Wolf Bros. & Co.*, 240 U.S. 251, 258 (1916); accord *Abbott* v. *Veasey*, 137 S. Ct. 612 (2017) (Roberts, C.J., respecting the denial of the petition for a writ of certiorari); *Virginia Military Inst.* v. *United States*, 508 U.S. 946 (1993) (Scalia, J., respecting the denial of the petition for a writ of certiorari). The court of appeals vacated the sanctions imposed by the SEC and remanded the matter to the Commission for further proceedings. Pet. App. 23. The Commission has not yet decided what sanctions, if any, are appropriate.

After the SEC resolves that issue, petitioner will have the opportunity to challenge the agency's remedial ruling in a court of appeals. Petitioner may then raise his current claims and any additional claims that are properly preserved in a single petition for a writ of certiorari seeking review of the final judgment against him. See, *e.g.*, *Major League Baseball Players Ass'n* v. *Garvey*, 532 U.S. 504, 508 n.1 (2001) (per curiam) (noting that the Court "ha[s] authority to consider questions determined in earlier stages of the litigation where certiorari is sought from" the most recent judgment).

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misplaced. In *Desai*, the court of appeals addressed whether a putative class was entitled to the presumption of reliance under *Affiliated Ute*. But that issue was not addressed by the decision below—or in any other case where the Commission was the plaintiff—because the Commission need not show reliance to prevail under Rule 10b-5. See *Morgan Keegan*, 678 F.3d at 1244.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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MAY 2018

No. 17-1077

In the Supreme Court of the United States

FRANCIS V. LORENZO,

Petitioner,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

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ARGUMENT

This case is an appropriate vehicle to resolve the question presented, which has been properly preserved and presented to this Court.

I. The SEC Does Not Dispute that the Circuits Are Split on the Question of Whether an Inadequate Claim for Misstatement Liability Can Be Repackaged as a Scheme Claim

The Securities and Exchange Commission (SEC or Commission) does not dispute that the circuit courts are split regarding the central question presented in this petition, namely whether a misstatement that does not meet the threshold for misstatement liability under Section 10(b) of the Securities and Exchange Act of 1934, 15 U.S.C. 78j(b)(2006)(the "Exchange Act") and SEC Rule 10b-5(b) 17 C.F.R 240.10b-5(b) can be repackaged as a fraudulent scheme claim under Section 17(a)(1) of the Securities Act of 1933, 15 U.S.C. 77q(a)(1)(2006) ("Securities Act") and Rule 10b-5(a) and (c), 17 C.F.R. 240.10b-5(a) and (c). As Petitioner's brief in support of this petition for certiorari noted, the circuits have split 3-2 on this question (Pet. 17-20). The Second, Eighth and Ninth Circuits have held that a misstatement alone cannot be the basis of a fraudulent scheme claim, while the DC Circuit and the Eleventh Circuit have held that a misstatement standing alone can be the basis of a fraudulent scheme claim. (Pet. 17-21)

The Commission attempts to paper over the circuit split by arguing that the circuits are not split on the scope of liability under Section 17(a)(1) of the Securities

Act (Brief for the Respondent in Opposition ("Opp.") at 8). However, merely because the circuit courts are not split with regards to Section 17(a)(1) of the Securities Act does not mean that the critical question of the scope of liability under Section 10(b) and Rule 10b-5(b) should not be resolved by the Court. The question regarding the scope of liability under this provision is an important and recurring question.

II. The Decisions that Petitioner Cites Reflecting the Majority Position Do Not Involve Different Conduct than the Conduct at Issue Here

The SEC argues that the circuit court cases Petitioner cites regarding the majority position are distinguishable because the cases supposedly involve different conduct than what is at issue here. (Opp. 8) However, the SEC's argument is mistaken. For example, *Lentell v. Merrill Lynch & Co.*, 396 F.3d 161, 177 (2d Cir. 2005) involved misstatements that are identical in character to the alleged misstatements in this matter in the sense that the statements in the *Lentell* case conveyed to investors a very positive assessment of the underlying investment. "The scheme had five elements common to research published on 24/7 Media and Interliant: (i) "the public issuance and maintenance of knowingly or recklessly false, bullish research reports"; (ii) the publication of false "BUY or ACCUMULATE recommendations" on 24/7 Media and Interliant; (iii) the setting of "profoundly unrealistic price targets for [those] stocks"" (*Lentell*, 296 F.3d at 165).

The SEC next argues that the Eighth Circuit's decision in *Desai v. Deutsche Bank Sec., Ltd.*, 573 F.3d

931, 939 (9th Cir. 2009) can be distinguished from this matter because the *Desai* decision "addressed whether a putative class was entitled to the presumption of reliance under [*Affiliated Ute Citizens v. United States*, 406 U.S. 128, 151 (1972)]" (Opp. 19 n.5) However, the SEC's argument has the analysis in *Desai* backward because the *Desai* Court had to first determine whether a fraudulent scheme case could be repackaged as an omission case before the court could reach the issue of whether a presumption of reliance could be had by the plaintiffs. "The presumption of reliance under *Affiliated Ute* is limited to cases that "can be characterized as . . . primarily alleg[ing] omissions." Therefore, if Investors' putative class action is not such a case, they cannot avail themselves of the *Affiliated Ute* presumption." (*Desai*, 573 F.3d at 940).

In fact, the *Desai* Court never had to reach the issue of whether a presumption of reliance could be had by the plaintiffs because the court determined that a scheme case could *not* be repackaged into a misrepresentation or omission case. Likewise, the conduct in *WPP Luxembourg Gamma Three Sarl v. Spot Runner, Inc.*, 655 F.3d 1039 (9th Cir. 2011) case is very similar to the conduct at issue here in that it involved alleged misrepresentations and omissions made to investors regarding material information about the company they were investing in. The plaintiffs in the *WPP* case alleged that the "[d]efendants carried out a plan, scheme and course of conduct which was intended to and did deceive WPP into continuing to invest in and support [Spot Runner] by concealing from WPP that the Founders of the Company and other Defendants were selling off their shares in large quantities." (*WPP*, 655 F.3d at 1057)

The *WPP* Court found "[a] defendant may only be liable as part of a fraudulent scheme based upon misrepresentations and omissions under Rules 10b-5(a) or (c) when the scheme also encompasses conduct beyond those misrepresentations or omissions." (*Ibid.*)

Contrary to the SEC's argument, the Ninth Circuit's decision in *Public Pension Fund Group v. KV Pharmaceutical Co.*, 679 F.3d 972 (8th Cir. 2012) is also on point because it involved misrepresentations made by the defendant to investors concerning material information about a company's business, including false and misleading statements about earnings. The *KV Pharma* Court held that a scheme liability claim must be based on conduct beyond just misrepresentations and omissions. The *KV Pharma* Court stated:

> Both the Second and the Ninth Circuits have held "[a] defendant may only be liable as part of a fraudulent scheme based upon misrepresentations and omissions under Rules 10b-5(a) or (c) when the scheme also encompasses conduct beyond those misrepresentations or omissions." *WPP Luxembourg Gamma Three Sarl v. Spot Runner, Inc.*, 655 F.3d 1039, 1057 (9th Cir.2011); *Lentell v. Merrill Lynch & Co.*, 396 F.3d 161, 177 (2d Cir. 2005) ("[W]here the sole basis for such claims is alleged misrepresentations or omissions, plaintiffs have not made out a market manipulation claim under Rule 10b-5(a) and (c)[.]"). We join the Second and Ninth Circuits in recognizing a scheme liability claim must be

> based on conduct beyond misrepresentations or omissions actionable under Rule 10b-5(b).

KV Pharma, 679 F.3d at 987.

III. Federal Court Holdings in Private Lawsuits Regarding the Elements of Antifraud Claims Also Apply to SEC Enforcement Actions

The SEC argues in opposition to the petition that the cases cited by Petitioner to demonstrate the circuit split have arisen out of suits by private plaintiffs rather than SEC enforcement cases. (Opp. 8). However, this argument is without merit because the same legal standards govern the adequacy of claims under the antifraud provisions of the federal securities laws whether the claims are brought by the SEC or brought by private plaintiffs. In fact, it is undisputed that the standards set out by the Court in *Janus Capital Group, Inc. v. First Derivative Traders*, 564 U.S. 13 (2011) for claims under Section 10(b) of the Exchange Act and Rule 10b-5(b) apply to SEC enforcement claims even though the *Janus* decision involved private litigation. Moreover, neither the majority nor the dissent in the court below ever argued that the cases from the Second, Eighth and Ninth Circuits (constituting the majority position) were inapplicable to this matter because those cases arose from private actions. Finally, the SEC's argument that the holdings in private lawsuits do not apply to SEC enforcement actions is particularly misplaced because throughout its opposition brief the SEC cites numerous decisions in private litigation when discussing the elements of claims under the federal antifraud provisions of the federal securities laws. (Opp. 8 - 15)

IV. The Commission Relies Primarily on Case Law that Predates the *Janus* Decision

The Court in *Janus* established a bright-line test to determine whether a person can be liable for false statements under Section 10(b) of the Exchange Act and Rule 10b-5(b) thereunder. In *Janus*, this Court held that a defendant can be liable for false statements under Rule 10b-5(b) only if the defendant was the "maker" of the false statements. *Janus*, 564 U.S. at 142. The Commission's argument that the decision below is consistent with *Janus* is incorrect. In its opposition the Commission discusses a number of cases that stand generally for the proposition that different provisions of the federal securities laws may overlap are not necessarily mutually exclusive. (Opp. 11- 12) However, the vast majority of the cases the SEC relies on predate the *Janus* decision and the few cases that the SEC cites that have come after *Janus* conflict with the position taken by a majority of the courts of appeals.

V. The SEC's Arguments Concerning the PSLRA Are Not Relevant

As discussed above, the Second, Eighth and Ninth Circuits have each held that a misstatement standing alone cannot be the basis of a fraudulent scheme claim. The Commission attempts to distinguish the decisions from the Second and Ninth Circuits by arguing that they involved cases that were brought by private plaintiffs and the cases were subject to the Private Securities Litigation Reform Act of 1995 ("PSLRA") Pub. L. No. 104-67, 109 Stat. 737. The PSLRA states that "if an allegation regarding the statement or omission is made on information and belief, the

complaint shall state with particularity all facts on which that belief is formed." 15 U.S.C. 78u-4(b)(1). However, none of the decisions cited by Petitioner when discussing the circuit split turn on the application of the PSLRA. In fact, neither the majority nor the dissent in the court below addressed the PSLRA in any way in their analysis of the various circuit court decisions addressing whether a defective misstatement claim can be repackaged as a scheme claim. Further, the SEC's argument regarding the PSLRA is misplaced because in this matter Petitioner is not challenging the adequacy of the Commission's fraud allegations as contained in the SEC's Order Instituting Proceedings, which is analogous to a complaint in federal court.

VI. Scheme Liability Was Not Presented as a Theory of Liability in Lorenzo's Administrative Proceeding

The SEC's attempt to impose scheme liability on Petitioner is particularly unfair, and constitutes a violation of his due process rights, because scheme liability was not a theory of liability that was pursued by the SEC in the administrative hearing. In fact, the administrative law judge's finding that Petitioner violated the antifraud provisions of the federal securities laws is based entirely on the theory that he made misrepresentations. The Administrative Law Judge found that "[t]he record shows that Frank Lorenzo violated the antifraud provisions *by making material misstatements and omissions in the emails*." (Pet. App. 113)(emphasis added) and "([i]n sum, it is concluded that Frank Lorenzo willfully violated the antifraud provisions of the Securities and Exchange Acts *by his material misrepresentations and omissions*

concerning W2E in the emails." (Pet. App. 114) (emphasis added).

The first time that a theory of scheme liability is raised is not at the administrative proceeding where Lorenzo had a chance to present testimony and other evidence but in the Commission's decision on appeal. "We also find that Lorenzo employed a "device, scheme, or artifice to defraud," in violation of Section 17(a)(1) and Rule 10b-5(a); that he engaged in an "act" that would operate as a fraud in violation of Rule 10b-5(c); and that his conduct was deceptive, as required by Section 10(b)." (Pet. App. 77)

As noted in Judge Kavanaugh's dissent below, the Commission's finding that Lorenzo's conduct amounted to a fraudulent scheme "was done without hearing from Lorenzo or any other witnesses" and that "the Commission simply swept the judge's factual and credibility findings under the rug." (Pet. App. 41). In this case, "the Commission rewrote the administrative law judge's factual findings to make those factual findings correspond to the legal conclusion that Lorenzo was guilty and deserving of a lifetime suspension." (*Ibid.*) The conduct by the Commission in this case denied Petitioner his right to a fair hearing (Pet. App 49) and the Commission should not be permitted to impose scheme liability on Lorenzo.

VII. The Question Presented is Critically Important and Properly Presented

The Commission also argues that this matter is allegedly in an interlocutory posture and this constitutes sufficient grounds for the Court to deny the petition. (Opp. 20) This argument is wrong for several

reasons. First, there is no bar to the Court's jurisdiction. The Court's jurisdiction in this matter is invoked under 28 U.S.C. § 1254(1) which provides "[c]ases in the courts of appeals may be reviewed by the Supreme Court by the following methods (1) By writ of certiorari granted upon the petition of any party to any civil or criminal case, before or after rendition of judgment or decree. . ."

Second, the DC Circuit has already issued a *definitive and final ruling* on the issue that is the subject of this petition for certiorari, namely the DC Circuit held that a defective misstatement claim under *Janus* can be repackaged as a scheme claim and brought under Section 17(a)(1), Section 10(b) and Rule 10b-5(a) and (c). By so holding the DC Circuit deepened an already existing split in the circuits. It is also noteworthy that the DC Circuit did *not* remand this matter to the Commission for additional fact finding and, in fact, the Commission has confirmed that there will be no additional fact finding when it issued its order requiring only legal briefs regarding sanctions be filed with the Commission itself. (*In re Lorenzo*, Securities Act Release No. 3-15211, 2017 WL 6349871 (Dec. 12, 2017). The Commission is not reopening the record or taking any additional testimony nor is it conducting a new hearing before an administrative law judge. The only issue that is pending before the Commission is what sanctions are to be imposed on Lorenzo for violations of Section 17(a)(1) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5(a) and (c). Regardless of how the Commission determines that sanctions issue the central holding of the Commission and the DC Circuit regarding Lorenzo's underlying violations of

Section 17(a)(1), Section 10(b) and Rule 10b-5(a) and (c) will not be changed.

In these circumstances this Court should grant the petition for a writ of certiorari. "[W]here there is an important and clear-cut issue of law that is fundamental to the further conduct of the case and that otherwise would qualify as a basis for certiorari, interlocutory status need not preclude review." *Randolph Cent. Sch. Dist. v. Aldrich*, 506 U.S. 965 (1992) (White, J., dissenting from denial of certiorari) (citations and internal quotation marks omitted).

Finally, the Court's jurisprudence under a different jurisdictional statute, 28 U.S.C. § 1291, is instructive here because the "Court has held that the requirement of finality is to be given a "practical, rather than a technical, construction." *Gillespie v. United States Steel Corp.*, 379 U.S. 148 (1964) citing *Cohen v. Beneficial Industrial Loan Corp.*, 337 U.S. 541, 545 (1949). Therefore, appealable finality is not limited just to matters where a judgment or order completely terminates a case. In *Gillespie*, this Court decided to hear an appeal because the Court's consideration of the inconvenience, cost and delay that would be involved if the appeal were denied all weighed in favor of the Court hearing the appeal. Similarly, here the SEC's argument that this matter should not be heard until the Commission imposes its sanctions and Petitioner again appeals to the DC Circuit and then files a new petition seeking a writ of certiorari is the very definition of inconvenience, cost and delay, particularly when the central legal issue regarding the applicability of scheme liability to Lorenzo has already been decided.

As discussed in the petition for a writ of certiorari the question presented in this petition arises frequently in SEC enforcement proceedings and in private securities litigation, including securities class action lawsuits. (Pet. 21) Private litigation and SEC enforcement actions often involve very significant liability and, in addition, SEC enforcement actions (like the one filed against Lorenzo) often seek to bar individuals from working in their chose profession in the securities industry.

The question presented in this case is of national importance, both for the SEC's enforcement program as well as for private plaintiffs. The question will reoccur and likely lead to a deepening of the circuit split if the Court does not grant Lorenzo's petition. In fact, federal district courts in circuits that have not ruled on the issue raised in this petition have already taken conflicting positions. *Compare Lautenberg Found. v. Madoff*, 2009 WL 2928913, at *12 (D.N.J. Sept. 9, 2009)("[c]ourts have generally held that '[a] Rule 10b–5(a) and/or (c) claim cannot be premised on the alleged misrepresentations or omissions that form the basis of a Rule 10b–5(b) claim'") *with SEC v. Benger*, 931 F. Supp. 2d 904, 905-06 (N.D. Ill. 2013) (misstatements can give rise to liability under the antifraud provisions even if the conduct in question does not amount to "making" a statement under *Janus*). *See also SEC v. Familant*, 910 F. Supp. 2d 83, 93-95 (D.D.C. 2012)(holding that misstatements can give rise to liability under the antifraud provisions even if the conduct in question does not amount to "making" a statement under *Janus*). The conflicts between the circuits and the disparate treatment of defendants based on what circuit they happen to be in

will only continue and grow more pronounced if the Court does not decide the important question presented in this petition.

CONCLUSION

For the foregoing reasons and those stated in the petition, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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May 23, 2018

No. 17-1077

In the Supreme Court of the United States

FRANCIS V. LORENZO,
Petitioner,

v.

SECURITIES AND EXCHANGE COMMISSION,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

JOINT APPENDIX

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August 20, 2018

Petition for Writ of Certiorari filed January 26, 2018
Petition for Writ of Certiorari granted June 18, 2018

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Order Instituting Administrative and Cease-And-Desist Proceedings Pursuant to Section 8A of the Securities Act of 1933, and Sections 15(b), 21B and 21C of the Securities Exchange Act of 1934, United States of America Before the Securities Exchange Commission, File No. 3-15211 (February 15, 2013) ..... JA 15

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Div. Ex. 34 – E-mails from Francis Lorenzo to Vishal Goolcharan and William Rothe, regarding "W2E Debenture Deal Points" (October 14, 2009) ..... JA 403

The following opinions, decisions, judgments, and orders have been omitted in printing this joint appendix because they appear on the following pages in the appendix to the Petition for Certiorari:

Appendix A Opinion and Dissenting Opinion of the United States Court of Appeals for the District of Columbia Circuit (September 29, 2017) . . . . . App. 1

Appendix B Opinion and Order Sustaining Disciplinary Action of the Securities and Exchange Commission (April 29, 2015) . . . . . App. 51

Appendix C Initial Decision of the Securities and Exchange Commission (December 31, 2013) . . . . . App. 98

RELEVANT DOCKET ENTRIES

U.S. Securities and Exchange Commission
Administrative Proceeding File No. 3-15211

Lorenzo, et al. v. Charles Vista, LLC

Release Date	Release Number	Other Release Numbers	Name of Document
Feb. 15, 2013	33-9385	34-68943	Order Instituting Administrative and Cease-and-Desist Proceedings and Notice of Hearing
Mar. 22, 2013	33-9385	34-68943	Resp G Lorenzo's Answer
Mar. 22, 2013	33-9385	34-68943	Resp Charles Vista's Answer
Aug. 13, 2013	33-9385	34-68943	Resps. Gregg C. Lorenzo and Charles Vista, LLC's Pre-Hearing Brief
Aug. 13, 2013			Division's Prehearing Brief
Sep. 3, 2013	AP-831		Stay Order
Sep. 6, 2013	AP-849		Prehearing Order
Oct. 30, 2013			Division's Proposed Findings of Fact and Conclusions of Law

Nov. 20, 2013	33-9480	34-70904	Order Making Findings and Imposing Remedial Sanctions and a Cease-and-Desist Order
Nov. 26, 2013			Francis V. Lorenzo's Proposed Findings of Fact and Conclusions of Law
Dec. 31, 2013	ID-544		Initial Decision
Jan. 27, 2014			Francis V. Lorenzo's Petition for Review of Initial Decision
Feb. 4, 2014			Division's Cross Petition for Review of Initial Decision
Feb. 18, 2014			Resp. Frank V. Lorenzo's Response to Division's Cross Petition for Review of Initial Decision
Feb. 20, 2014	34-71584		Order Granting Petitions for Review and Scheduling Briefs
Mar. 24, 2014			Brief in Support of Petition for Review of Respondent Francis V. Lorenzo

Apr. 22, 2014			Division's Memorandum of Law in Opposition to Respondent Francis V. Lorenzo's Appeal, and in Support of the Division's Cross-Appeal, from Initial Decision Release No. 544
May 7, 2014			Reply Brief in Support of Petition for Review of Respondent Francis V. Lorenzo and in Opposition to the Division's Cross-Appeal
Aug. 15, 2014	34-72856		Order Appointing Tax Administrator
Jan. 16, 2015			Respondent Frank Lorenzo's Notice of Supplemental Authority
Jan. 21, 2015			Division's Response to Respondent Frank Lorenzo's Notice of Supplemental Authority
Feb. 24, 2015	33-9732	34-74364	Order Scheduling Oral Argument

Mar. 30, 2015	34-74607		Notice of Proposed Plan of Distribution and Opportunity for Comment
Apr. 29, 2015	33-9762	34-74836	Cease-and-Desist Proceeding
May 12, 2015			Motion for Reconsideration Submitted On Behalf of Respondent Francis V. Lorenzo
May 28, 2015	34-75059		Extension Order
Jun. 3, 2015	33-9803	34-75103	Order Denying Lorenzo's Motion for Reconsideration
Jan. 5, 2016	34-76837		Notice of Amended Proposed Plan of Distribution and Opportunity for Comment
Dec. 12, 2017	33-10447	34-82307	Order Scheduling Briefs
Jan. 9, 2018			Division's Opposition to Respondent Francis V. Lorenzo's Motion to Stay the Commission's Order Scheduling Briefs

Jan. 11, 2018			Respondent Francis V. Lorenzo's Brief Regarding Sanctions
Jan. 29, 2018			Division's Opposition to Respondent Lorenzo's Brief Regarding Sanctions, w/Ex. 1
Feb. 9, 2018	34-82677		Order Approving Amended Plan of Distribution
Feb. 21, 2018	33-10460	34-82755	Order Denying Stay
Feb. 26, 2018			Respondent Lorenzo's Reply Brief Regarding Sanctions
Jun. 25, 2018	34-83502		Order Directing Disbursement of Fair Fund

RELEVANT DOCKET ENTRIES

United States Court of Appeals for District of Columbia Circuit
No. 15-1202

Francis Lorenzo v. SEC

07/01/2015	PETITION FOR REVIEW CASE docketed. [15-1202] [Entered: 07/09/2015 04:00 PM]
07/01/2015	PETITION FOR REVIEW filed [1561795] by Francis V. Lorenzo of a decision by federal agency [Service Date: 07/01/2015] Disclosure Statement: Attached; Certificate of Parties: Not Applicable to this Filing. [15-1202] [Entered: 07/09/2015 04:03 PM]
07/09/2015	CERTIFIED COPY [1561798] of Petition for Review sent to respondent [1561795-2] [15-1202] [Entered: 07/09/2015 04:05 PM]
07/09/2015	CLERK'S ORDER filed [1561800] directing party to file initial submissions: PETITIONER docketing statement due 08/10/2015. PETITIONER certificate as to parties, etc. due 08/10/2015. PETITIONER statement of issues due 08/10/2015. PETITIONER underlying decision due 08/10/2015. PETITIONER deferred appendix statement due 08/10/2015. PETITIONER procedural motions due 08/10/2015. PETITIONER dispositive motions due 08/24/2015;

	directing party to file initial submissions: RESPONDENT entry of appearance due 08/10/2015. RESPONDENT procedural motions due 08/10/2015. RESPONDENT certified index to record due 08/24/2015. RESPONDENT dispositive motions due 08/24/2015 [15-1202] [Entered: 07/09/2015 04:07 PM]
07/23/2015	ENTRY OF APPEARANCE [1563997] filed by Benjamin Lawrence Schiffrin on behalf of Respondent SEC. [15-1202] (Schiffrin, Benjamin) [Entered: 07/23/2015 11:57 AM]
08/24/2015	CERTIFIED INDEX TO RECORD [1569373] filed by SEC [Service Date: 08/24/2015] [15-1202] (Schiffrin, Benjamin) [Entered: 08/24/2015 12:56 PM]
08/25/2015	CERTIFICATE AS TO PARTIES, RULINGS AND RELATED CASES [1569704] filed by Francis V. Lorenzo [Service Date: 08/25/2015] [15-1202] (Heim, Robert) [Entered: 08/25/2015 04:33 PM]
08/25/2015	DOCKETING STATEMENT [1569707] filed by Francis V. Lorenzo [Service Date: 08/25/2015] [15-1202] (Heim, Robert) [Entered: 08/25/2015 04:34 PM]
08/25/2015	STATEMENT OF ISSUES [1569709] filed by Francis V. Lorenzo [Service Date: 08/25/2015] [15-1202] (Heim, Robert) [Entered: 08/25/2015 04:36 PM]

08/25/2015	STATEMENT OF INTENT REGARDING APPENDIX DEFERRAL [1569712] filed by Francis V. Lorenzo [Service Date: 08/25/2015] Intent: AppxDeferred [15-1202] (Heim, Robert) [Entered: 08/25/2015 04:39 PM]
08/25/2015	UNDERLYING DECISION IN CASE submitted [1569713] by Francis V. Lorenzo [Service Date: 08/25/2015] [15-1202] (Heim, Robert) [Entered: 08/25/2015 04:41 PM]
08/25/2015	UNOPPOSED MOTION filed [1569714] by Francis V. Lorenzo to extend time to file initial submissions to 08/25/2015. [Service Date: 08/25/2015] Pages: 1-10. [15-1202] (Heim, Robert) [Entered: 08/25/2015 04:47 PM]
08/26/2015	CLERK'S ORDER filed [1569758] granting motion to extend time [1569714-2]. Petitioner's initial submissions are deemed timely filed. [15-1202] [Entered: 08/26/2015 10:51 AM]
09/10/2015	CLERK'S ORDER [1572271] filed setting briefing schedule: PETITIONER Brief due 10/20/2015. RESPONDENT Brief due on 11/19/2015. PETITIONER Reply Brief due 12/03/2015. DEFERRED APPENDIX due 12/10/2015. PETITIONER Final Brief due 12/24/2015. RESPONDENT Final Brief due on 12/24/2015. PETITIONER Final Reply Brief due 12/24/2015 [15-1202] [Entered: 09/10/2015 10:47 AM]

10/20/2015	PETITIONER BRIEF [1579035] filed by Francis V. Lorenzo [Service Date: 10/20/2015] Length of Brief: 6,344. [15-1202] (Heim, Robert) [Entered: 10/20/2015 03:42 PM]
11/19/2015	RESPONDENT BRIEF [1584433] filed by SEC [Service Date: 11/19/2015] Length of Brief: 9,965 words. [15-1202] (Schiffrin, Benjamin) [Entered: 11/19/2015 02:30 PM]
12/02/2015	NOTICE [1586456] filed by Francis V. Lorenzo to substitute attorney Joshua Rose substituted by Steven L. Herrick [Service Date: 12/02/2015] [15-1202] (Herrick, Steven) [Entered: 12/02/2015 05:48 PM]
12/03/2015	PETITIONER REPLY BRIEF [1586680] filed by Francis V. Lorenzo [Service Date: 12/03/2015] Length of Brief: 3,709. [15-1202] (Heim, Robert) [Entered: 12/03/2015 03:41 PM]
12/10/2015	*JOINT* APPENDIX [1587893] filed by Francis V. Lorenzo and SEC. [Volumes: 2] [Service Date: 12/10/2010] [15-1202] (Heim, Robert) [Entered: 12/10/2015 12:00 PM]
12/24/2015	RESPONDENT FINAL BRIEF [1590524] filed by SEC [Service Date: 12/24/2015] Length of Brief: 9,867 Words. [15-1202] (Schiffrin, Benjamin) [Entered: 12/24/2015 08:49 AM]

12/24/2015	PETITIONER FINAL BRIEF [1590601] filed by Francis V. Lorenzo [Service Date: 12/24/2015] Length of Brief: 6,344. [15-1202] (Heim, Robert) [Entered: 12/24/2015 11:18 AM]
12/24/2015	PETITIONER FINAL REPLY BRIEF [1590603] filed by Francis V. Lorenzo [Service Date: 12/24/2015] Length of Brief: 3,709. [15-1202] (Heim, Robert) [Entered: 12/24/2015 11:19 AM]
01/13/2016	LETTER [1593301] filed by SEC advising of arguing counsel's availability for oral argument. [Service Date: 01/13/2016] [15-1202] (Schiffrin, Benjamin) [Entered: 01/13/2016 12:29 PM]
02/17/2016	LETTER [1599206] filed by Francis V. Lorenzo advising of arguing counsel's availability for oral argument. [Service Date: 02/17/2016] [15-1202] (Heim, Robert) [Entered: 02/17/2016 02:45 PM]
03/16/2016	LETTER [1604245] filed by Francis V. Lorenzo advising of arguing counsel's availability for oral argument. [Service Date: 03/16/2016] [15-1202] (Heim, Robert) [Entered: 03/16/2016 02:55 PM]
04/22/2016	LETTER [1610060] filed by Francis V. Lorenzo advising of arguing counsel's availability for oral argument. [Service Date: 04/22/2016] [15-1202] (Heim, Robert) [Entered: 04/22/2016 04:01 PM]

04/26/2016	NOTICE [1610406] filed by Francis V. Lorenzo to substitute attorney Steven L. Herrick substituted by Stephanie Rapp-Tully [Service Date: 04/26/2016] [15-1202] (Rapp-Tully, Stephanie) [Entered: 04/26/2016 09:26 AM]
06/17/2016	CLERK'S ORDER [1620136] filed scheduling oral argument on Thursday, 09/15/2016. [15-1202] [Entered: 06/17/2016 04:35 PM]
06/21/2016	ENTRY OF APPEARANCE [1620779] filed by Martin V. Totaro on behalf of Respondent SEC. [15-1202] (Totaro, Martin) [Entered: 06/21/2016 02:56 PM]
08/19/2016	LETTER [1631250] filed by SEC pursuant to FRAP 28j advising of additional authorities [Service Date: 08/19/2016] [15-1202] (Totaro, Martin) [Entered: 08/19/2016 02:35 PM]
09/02/2016	PER CURIAM ORDER [1633721] filed allocating oral argument time as follows: Petitioner - 15 Minutes, Respondent - 15 Minutes. One counsel per side to argue; directing party to file Form 72 notice of arguing attorney by 09/08/2016 [15-1202] [Entered: 09/02/2016 04:08 PM]
09/02/2016	FORM 72 submitted by arguing attorney, Martin Totaro, on behalf of Respondent SEC *(For Internal Use Only: Form is restricted to protect counsel's personal contact information)*. [15-1202] (Totaro, Martin) [Entered: 09/02/2016 05:10 PM]

09/08/2016	FORM 72 submitted by arguing attorney, Robert Heim, on behalf of Petitioner Francis V. Lorenzo *(For Internal Use Only: Form is restricted to protect counsel's personal contact information).* [15-1202] (Heim, Robert) [Entered: 09/08/2016 12:05 PM]
09/15/2016	ORAL ARGUMENT HELD before Judges Griffith, Kavanaugh and Srinivasan. [15-1202] [Entered: 09/16/2016 04:34 PM]
02/23/2017	LETTER [1662826] pursuant to FRAP 28j advising of additional authorities filed by SEC [Service Date: 02/23/2016] [15-1202] (Totaro, Martin) [Entered: 02/23/2017 08:09 PM]
07/06/2017	TRANSCRIPT [1682985] of oral argument [15-1202] [Entered: 07/07/2017 12:36 PM]
07/28/2017	NOTICE [1686390] to substitute attorney Stephanie Rapp-Tully substituted by Donna Williams Rucker filed by Francis V. Lorenzo [Service Date: 07/28/2017] [15-1202] (Rucker, Donna) [Entered: 07/28/2017 04:20 PM]
09/29/2017	PER CURIAM JUDGMENT [1695569] filed that the petition for review be granted in part, the sanctions imposed by the Commission be vacated, and the matter be remanded for further consideration for the reasons in the accompanying opinion . Before Judges:

	Griffith, Kavanaugh, and Srinivasan. [15-1202] [Entered: 09/29/2017 09:56 AM]
09/29/2017	OPINION [1695572] filed (Pages: 34) for the Court by Judge Srinivasan, DISSENTING OPINION (Pages: 12) by Judge Kavanaugh. [15-1202] [Entered: 09/29/2017 09:59 AM]
09/29/2017	CLERK'S ORDER [1695574] filed withholding issuance of the mandate. [15-1202] [Entered: 09/29/2017 10:00 AM]
11/21/2017	MANDATE ISSUED to Securities and Exchange Commission. [15-1202] [Entered: 11/21/2017 01:42 PM]
12/26/2017	LETTER [1711038] received from the Clerk of the Supreme Court of the United States notifying this court that the time for filing a petition for writ of certiorari has been extended to: 01/26/2018. [15-1202] [Entered: 01/02/2018 09:35 AM]
01/31/2018	LETTER [1716356] received from the Clerk of the Supreme Court of the United States notifying this court of the following activity in the case before it: A petition for writ of certiorari was filed and placed on the docket on 01/31/2018 as No. 17-1077. [15-1202] [Entered: 02/02/2018 06:21 PM]
06/18/2018	LETTER [1736534] received from the Clerk of the Supreme Court of the United States notifying this court of the following activity in case No. 17-1077:

	The petition for writ of certiorari was granted on 06/18/2018. [15-1202] [Entered: 06/18/2018 03:19 PM]

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 9385 / February 15, 2013

SECURITIES EXCHANGE ACT OF 1934
Release No. 68943 / February 15, 2013

ADMINISTRATIVE PROCEEDING
File No. 3-15211

[Filed February 15, 2013]

In the Matter of	)
	)
GREGG C. LORENZO,	)
FRANCIS V. LORENZO, and	)
CHARLES VISTA, LLC,	)
	)
Respondents.	)
	)

ORDER INSTITUTING ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTION 8A OF THE SECURITIES ACT OF 1933, AND SECTIONS 15(b), 21B AND 21C OF THE SECURITIES EXCHANGE ACT OF 1934

I.

The Securities and Exchange Commission ("Commission" or "SEC") deems it appropriate and in the public interest that public administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 8A of the Securities Act

of 1933 ("Securities Act"), and Sections 15(b), 21B and 21C of the Securities Exchange Act of 1934 ("Exchange Act") against Gregg C. Lorenzo ("Gregg Lorenzo"), Francis V. Lorenzo ("Frank Lorenzo"), and Charles Vista, LLC ("Charles Vista") (collectively, "Respondents").

II.

After an investigation, the Division of Enforcement alleges that:

1. Beginning in or about September 2009, Gregg Lorenzo, Frank Lorenzo, and Charles Vista, a broker-dealer controlled by Gregg Lorenzo, made fraudulent misrepresentations to several customers of Charles Vista to induce them to invest in convertible debentures issued by a start-up waste management company called Waste2Energy Holdings, Inc. ("W2E").

2. In telephone conversations with at least three Charles Vista customers, Gregg Lorenzo attempted to convince them to purchase the highly risky W2E debentures by (a) making false, misleading, and unfounded statements designed to create the impression that the debentures were less risky than they actually were, and (b) making unfounded positive predictions about the upside of the investment, including the future price of W2E stock and the likelihood of it trading on the NASDAQ.

3. Frank Lorenzo also engaged in fraudulent efforts to sell the W2E debentures to Charles

Vista customers, by sending at least two Charles Vista customers emails containing false and/or misleading statements concerning W2E's assets and alleged contracts.

4. Charles Vista committed fraud through the actions of Gregg Lorenzo and Frank Lorenzo, described above.

A. RESPONDENTS

Gregg Lorenzo

5. Gregg Lorenzo, age 30, is the president and indirect owner of Charles Vista, a registered broker-dealer doing business in Staten Island, New York. Lorenzo's indirect ownership stems from his status as the sole shareholder and managing member of GJL Holdings, LLC ("GJL"), a New York limited liability company that wholly owns Charles Vista. From April 2002 to the present, Gregg Lorenzo has been a registered representative associated with various broker-dealers registered with the Commission, and is currently associated with Charles Vista. Lorenzo holds the Series 7, Series 24, and Series 63 licenses. He resides in Staten Island, New York.

6. In September 2005, Gregg Lorenzo joined Mercer Capital ("Mercer"), a now defunct New York broker-dealer. Shortly afterward, Gregg Lorenzo settled civil fraud and other charges with the State of Montana arising from his prior employment at a different brokerage firm. He also agreed to withdraw his securities license in Montana for two years and pay a $35,000 fine. In a separate matter, in February 2007, the National Association of Securities Dealers found

that Mercer and Gregg Lorenzo had violated agreements with the New Jersey and Indiana securities authorities, which had imposed strict supervision requirements on Gregg Lorenzo at Mercer.

7. In January 2008, Gregg Lorenzo left Mercer and joined John Thomas Financial, a New York-based registered broker-dealer. In February 2008, Gregg Lorenzo and John Thomas Financial entered into a consent order with the Iowa Securities and Regulated Industries Bureau requiring heightened supervision of Gregg Lorenzo and precluding him from performing supervisory responsibilities for two years.

8. In February 2009, through an entity that he owned, Gregg Lorenzo purchased a registered broker-dealer shell company called DC Evans and Company LLC ("DC Evans") and renamed it Charles Vista, LLC. Gregg Lorenzo continues to operate Charles Vista as a broker-dealer in Staten Island, N.Y. Although the indirect owner of the firm, Gregg Lorenzo officially has no managerial title and is listed only as a registered representative at Charles Vista. Despite his lack of a managerial title, however, Gregg Lorenzo in fact controlled Charles Vista.

9. In a July 16, 2009 Agreement and Order with the Idaho Department of Finance, *Idaho v. John Thomas Financial et al.*, Docket No. 2008-7-11, the Idaho Securities Division sanctioned John Thomas Financial and Gregg Lorenzo, among others, for negligently failing to disclose the Iowa consent order in his form U-4. The order directed Gregg Lorenzo to withdraw his application for registration as an investment adviser representative and to pay a civil penalty of $1,250.

10. On December 16, 2009, the Financial Industry Regulatory Authority ("FINRA") denied Charles Vista's application to transfer membership from DC Evans to Charles Vista. On August 10, 2010, FINRA upheld its earlier decision, citing Lorenzo's regulatory history.

Frank Lorenzo

11. Frank Lorenzo, age 51, resides in Westwood, New Jersey and is currently registered with Hunter Wise Securities, LLC, a registered broker-dealer based in Irvine, California. Frank Lorenzo works at the firm's New York City office. Frank Lorenzo holds Series 7 and 63 licenses. He began working at Mercer Capital in February 2007 and then followed Gregg Lorenzo to John Thomas Financial and Charles Vista. Frank Lorenzo acted as an investment banker at Mercer Capital, John Thomas Financial and Charles Vista.

Charles Vista

12. Charles Vista is a registered broker-dealer controlled by Gregg Lorenzo. Frank Lorenzo was the head of investment banking from the opening of the firm until his departure in January 2010.

B. OTHER RELEVANT ENTITIES

13. According to W2E's SEC filings,W2E is a Delaware corporation formed in 2008 as Maven Media Holdings, Inc. ("Maven Media"). In May 2009, Maven Media's wholly-owned subsidiary, Waste2Energy Acquisition Co., acquired Waste2Energy, Inc., a privately held Delaware corporation that held 95% of the issued and outstanding shares of EnerWaste International Corporation ("EWI"), a company that

manufactured a so-called "Batch Oxidation System" for converting waste into energy. EWI owned 50% of EnerWaste Europe, Ltd. ("EWE"), a company based in Iceland that operated a waste processing facility in that country. In April 2008, Waste2Energy, Inc. formed a wholly owned subsidiary, EnerWaste, Inc. to acquire the other 50% of the stock of EWE. In July 2009, Maven Media (which prior to the acquisition of Waste2Energy, Inc. had been a shell corporation with publicly registered stock) changed its name to Waste2Energy Holdings, Inc. Shortly thereafter, W2E's stock began to be quoted on the Over-The-Counter Bulletin Board ("OTCBB").

C. W2E's OPERATIONS AND FINANCIAL CONDITION

14. According to W2E's SEC filings, Waste2Energy, Inc. was incorporated in Delaware on April 10, 2007. On August 27, 2007, Waste2Energy, Inc. filed a Form D notice that it was engaged in a $6 million private offering of securities pursuant to Rule 506 of Regulation D, 17 C.F.R. § 230.506. According to its September 4, 2007 private placement memorandum, Waste2Energy, Inc. was formed to acquire 95% of the "issued and outstanding shares of capital stock" of EWI.

15. According to W2E's SEC filings, Waste2Energy, Inc. completed the EWI acquisition in or about November 2007, thereby acquiring 50% of EWE. Through EnerWaste, Inc., Waste2Energy acquired the remaining 50% of the stock of EWE. Waste2Energy, Inc.'s total purchase price for EWE was $8 million, which it paid in roughly equal parts in cash, W2E stock and a W2E promissory note.

16. According to W2E's SEC filings, when Waste2Energy, Inc. acquired EWE, EWE had a contract with Ascot Environmental Ltd. ("Ascot") to develop a waste-to-energy facility in the Dargaval area of Dumfries, Scotland. In 2008, W2E took over this contract through its Isle of Man subsidiary, Waste2 Energy Limited.

17. On June 30, 2009, W2E filed a Form 8-K with the SEC that contained its first "unaudited" public post-merger financial statements. The financial statements stated, among other things, that, as of December 31, 2008, W2E had total assets of $13,987,764, total liabilities of $9,563,673, and that W2E "had been operating at a substantial operating loss each year since inception." Of the nearly $14 million in assets as of December 31, 2008, W2E attributed $10 million to "intangibles" (including a $1.9 million deferred tax liability), $0.5 million to goodwill, and $3 million to "cost and estimated earnings of billings on uncompleted contracts." The Form 8-K also disclosed that EWE had been placed in involuntary receivership in February 2009. The filing listed $28,171 in cash as of December 31, 2008 and further disclosed that W2E's current business operations were dependent on generating substantial revenues from one customer, Ascot, which subjected W2E to "significant financial and other risks in the operation of our business." The anticipated revenue from the contract with Ascot, at the time it was entered into, was less than $15 million, and by the time the Form 8-K was filed in June 2009, the contract was operating at a net loss for W2E. Furthermore, by September 2009, W2E had received all, or virtually all, of the payments it was entitled to under its contract with Ascot.

18. On October 1, 2009, W2E filed an amended Form 8-K ("Form 8K/A") and its Form 10-Q for the period ended June 30, 2009. The financial statements contained in the October 1 filings included "unaudited" numbers for the period ended June 30, 2009 and, apparently, audited numbers for the period ended March 31, 2009. For the period ended March 31, 2009, W2E reported total assets of $367,581 (including $27,360 in cash), total liabilities of $6,676,163, and an operating loss of $1,972,637. For the period ended June 30, 2009, W2E reported total assets of $660,408 (including $54,543 in cash), total liabilities of $3,942,356, and an operating loss of $1.5 million. The alleged $11 million in intangible assets and goodwill that W2E had reported in the Form 8-K that it filed June 30, 2009 were no longer included on the balance sheet that appeared in its October 1, 2009 Form 10-Q and Form 8-K/A filings.

19. W2E's October 1, 2009 Form 8-K/A explained the complete write-off of $11 million in intangibles and goodwill as follows:

> In January 2009, the Company engaged a consultant to assist in the evaluation of the Dargavel project [for Ascot] due to continued delays and concerns over the design and plans for the facility, as well as the progress and ability to complete the project in accordance with the contract. The initial plans, designs, and knowhow that were the foundation of the project plan also served as the basis of the Technology assets we acquired with the purchase of [EWE]. The conclusion reached was that the Company

> needed to completely change the project plans, technology and controls that would enable the company to deliver the project according to the contract specifications. As a result, management made a determination that the value of the assets acquired were of no value and the Company's IP platform would be built on a new set of plans, design specifications and technology that was developed starting in January through the expected conclusion of the project in late 2009. As a result, an impairment charge in the amount of $10,538,029 was recorded to write-off the value of the Technology.
>
> Additionally, when the Company acquired [EWE], Goodwill was assigned based on the value of the workforce. At the time of the Iceland economic collapse and subsequent termination of the contract between EWE and the company, and the signing of the new contract with another Company subsidiary, the majority of the workforce where the value was place did not continue on with the Dargavel project or any other efforts supporting the continued development of the Technology and knowhow of the business. As a result of the above, management determined that Goodwill was impaired and an impairment in the amount of $496,594 was recorded to write-off the value of the Goodwill.

20. On November 16, 2009, W2E filed a Form 10-Q for the period ending September 30, 2009. In this

filing, W2E reported that as of September 30, 2009, the value of all of W2E's assets was $905,582, its total liabilities were $6,510,247, and it had an accumulated deficit of $23,675,381. The value of contracts receivable was listed as zero and unbilled amounts due on uncompleted contracts was $499,857.

D. W2E's $15 MILLION DEBENTURE OFFERING

21. From in or about September 2009 through May 2010, Gregg Lorenzo's firm, Charles Vista, was the exclusive placement agent for an issuance of 12% W2E debentures, with a maximum issuance amount of $15 million (the "Debentures"). The Debentures were convertible to W2E stock.

22. Charles Vista's financial interest in the Debentures offering was considerable. According to documents attached to some of W2E's SEC filings, Charles Vista was to receive (1) a 10% "commission" on the gross proceeds of all Debentures sales; (2) a 3% "expense allowance" on the same proceeds; (3) a consulting fee of $10,000 per month for twelve months starting "at the initial closing" of the Debentures offering; (4) an "investment banking fee equal to $125,000 for each $2,500,000 of Debentures sold, up to a total of $750,000"; (5) another 13% commission/ expense allowance "upon the exercise of the Warrants issued to the purchasers of the Debentures"; and (6) a "warrant to purchase up to 4.5 %" of W2E's outstanding shares "proportionate to [the] amount of Debentures sold" (at a $.01 exercise price).

23. Charles Vista sent potential investors written materials concerning W2E and the Debentures, including a lengthy private offering memorandum

("POM") prepared by W2E, Charles Vista, and their respective attorneys. The POM stated that the Debentures "are highly speculative in nature, involve a high degree of risk and should be purchased only by persons who can afford to lose their entire investment." The POM also listed a number of individual risks concerning investment in the Debentures.

24. In addition to the POM, investors received, and were required to sign, a subscription agreement that contained risk disclosures similar to the POM.

E. GREGG LORENZO'S FALSE STATEMENTS TO INVESTORS

25. Gregg Lorenzo personally attempted to sell the Debentures to numerous potential investors. In his oral sales pitches to at least three potential investors, Lorenzo made false and misleading statements designed to (i) ameliorate concerns about the investment's downside risk by misrepresenting W2E's financial condition and business prospects; and (ii) make the Debentures' stock conversion feature appear valuable by making baseless predictions about the future price of the company's stock and its future listing on a major exchange.

INVESTOR A

26. Gregg Lorenzo spoke to Investor A several times, including in a recorded telephone conversation on September 23, 2009. During that telephone conversation, Gregg Lorenzo knowingly or recklessly made the following materially false and/or misleading statements to induce Investor A to purchase the Debentures:

(a) Discussing W2E, Gregg Lorenzo falsely told Investor A that "right now they have a contract. They have a contract that's totaling $100 to $200 million, but I don't know how fast they're going to get that money, so I can't really say what type of cash roll they're going to generate."

(b) Gregg Lorenzo made the following statements to assure Investor A that investment in the Debentures was not as risky as the written risk disclosures had made it seem, and that Investor A will "get [his] money back" because W2E allegedly would have "$7 million" in cash to repay debenture holders regardless of its future revenue:

> But I got to tell you this. If this is a private placement, and there weren't protective features in the transaction, and it wasn't somewhat of an insurance policy, I would tell you, you're right, don't do it. But the fact that there is and you get the benefit of having a debenture and it being senior and being in front of everything else that this company has, accrued salary, shareholders, you name it, and it's the only debt the company will have on their book, I mean, I – it's hard really – it's hard to really put this into a very, very risky category despite what those documents read because at the end of the day, . . . this company is still going to have close to $7 million in the bank, and I'm talking no revenue at all.
>
> So I understand where you're coming from, but there is nothing in this market, there is nothing in this industry in my opinion with

you being a client of my firm that can do what this deal can do for you because I'm telling you now, with our reputation on the line, me saying this to you, if you don't want to convert because you feel that the market is not there, the company hasn't executed, you are getting your money back.

They're going to be left with these – close to or exactly the amount of cash that they were given. Now again, I, I'm going to hold them accountable to pay this money back out of revenue.

* * *

But I look at it like this. I'll be honest with you. Based on their burn rate, and what they're going to get left with, they're still going to have close to $7 million in cash. If I have to raise a measly 8 million bucks to help them at worst case scenario, I'm not worried about that. These are the – this is the worst case scenario that I can possibly think of. I just – I just don't see that happening. I, you know, I, I'm sorry. And if they do, I am prepared as the chairman of Charles Vista to make sure that the investors get paid back.

* * *

You know, the odds of you being successful are, are highly likely.

* * *

I also want you to know that this is a very, very strong transaction.

* * *

I will make sure that you get paid back your money in this transaction. I don't believe that you will even take back your money. I have full confidence you will convert this note into stock at a dollar because the stock will be trading at a significant premium with liquidity because the company has executed their business plan.

* * *

And you're going to have a year to watch it for yourself. I don't have to say anything. The proof will be in the pudding, and you'll be able to decide what you want to do. It's like, it's like being able to place a bet and making a decision if you want to keep that bet a year from now.

* * *

But you are getting your money back, and you're going to get your final interest payment, and you are getting your warrants up front, and you'll be able to decide if you want to keep going. That [other] stock cannot offer you that. No public stock can offer you that. It's just not out there.

(c) During the September 23, 2009 telephone call with investor A, Gregg Lorenzo also made the following baseless prediction regarding W2E's alleged

future listing on NASDAQ: "I believe [W2E] will be a NASDAQ trading stock within 12 months. I believe they will meet the listing requirements."

(d) On the same call, Gregg Lorenzo also made equally baseless statements concerning the future price of W2E's stock, into which the Debentures could be converted. He told Investor A that "I have full confidence you will convert this note into stock at a dollar because the stock will be trading at a significant premium with liquidity because [W2E] has executed their business plan." Later in the call, while trying to convince Investor A to invest $75,000 more than he already had decided to invest in the Debentures, Gregg Lorenzo stated that an additional $75,000 means "150,000 more shares in a company that could potentially be $5 to $10 a share within 12 months. And that's what I'm looking at. You're giving up on that, and I just don't want you to do that. 150,000 shares at $5 is almost a million dollars to you. It's 700, it's close to $750,000."

(e) Gregg Lorenzo also told Investor A on September 23, 2009 that he was in possession of favorable non-public information concerning W2E, stating: "I can tell you things that are not even public yet that I shouldn't tell you, but it's not going to make a difference. You're going to want to see these things happen."

(f) Finally, Lorenzo falsely told Investor A on September 23, 2009 that the "debenture [was] senior and being in front of everything else that [W2E] has, accrued salary, shareholders, you name it, and it's the only debt the company will have on their book."

27. Gregg Lorenzo had no reasonable basis for making the statements set forth in paragraph 26 above because, as he knew or recklessly disregarded:

(a) W2E never had a contract for "$100 to $200 million"; its only substantial contract, with Ascot, was worth less than $15 million at the outset, and as of September 23, 2009, when Lorenzo had the call with Investor A, W2E already had received all, or virtually all, payments due under that contract.

(b) W2E's last public filing prior to September 23, 2009 — its May 28, 2009 Form 8-K — reported, not that the company had "$7 million in the bank" as Lorenzo told Investor A, but that (i) as of December 31, 2008, W2E had only $28,171 in cash; and (ii) as of May 28, 2009, the company had only $194,369 in cash. Furthermore, W2E's Form 10-Q for the period that ended June 30, 2009 (filed October 1, 2009) reported that the company had only $54,543 in cash and less than $700,000 in total assets; and W2E's Form 10-Q for the period ended September 30, 2009 (filed November 16, 2009) reported total assets of $905,582, total liabilities of $6,510,247, an accumulated deficit of $23,675,381, contracts receivable valued at zero, and unbilled amounts due on uncompleted contracts at $499,857.

(c) and (d) W2E was an extremely speculative stock — it was a start-up company at an early stage of development, and its financial condition was extremely precarious. Furthermore, on September 23, 2009 — the day that Gregg Lorenzo made his stock price and NASDAQ listing predictions to Investor A — W2E filed a Form 8-K reporting that on August 20, 2009, FINRA had notified the company that if it did not file a

delinquent Form 10-Q by September 21, its stock could be de-listed from the OTCBB, a trading venue with much less demanding listing requirements than the NASDAQ. In addition, the POM reported that (1) the "sole member of our board of directors was a defendant in prior litigation arising [sic] alleging violation of the Federal Securities laws, which may prevent or make more difficult listing on a national exchange and/or NASDAQ"; and, after further describing the litigation, (2) "[t]here can be no assurance that [the Director's] actions and/or involvement in the prior litigation will not negatively impact and/or prevent [W2E's] ability to be listed on an exchange and/or NASDAQ, even if [W2E] were to meet such listing qualifications, which it will not for the foreseeable future."

(e) No "non-public information concerning W2E" existed, and none of W2E's public statements after September 23, 2009 indicate that any such undisclosed favorable information about the company existed on or around September 23, 2009.

(f) As Gregg Lorenzo knew, as of September 23, 2009, W2E had millions of dollars in debt on its books that was senior to the debt W2E was issuing through the Debentures offering.

28. On September 25, 2009 and October 1, 2009, Investor A invested a total of $225,000 in the Debentures.

INVESTOR B

29. In or about September, 2009, Gregg Lorenzo spoke to Investor B concerning the Debentures. During his conversations with Investor B, Lorenzo knowingly or recklessly falsely told investor B that he would make

several times his money if he invested in the Debentures.

30. After speaking to Gregg Lorenzo, Investor B invested $150,000 in the Debentures.

31. Even after Investor B invested $150,000 in the Debentures, Gregg Lorenzo continued to solicit additional money. When Investor B asked Gregg Lorenzo to send him more information, he received an e-mail dated October 2, 2009 that purported to "summarize several key points of the Waste2Energy Holdings, Inc. Debenture Offering." After he received this e-mail, which contained several misrepresentations about W2 (as described in paragraphs 34 through 39 below), Investor B made another $200,000 investment in the Debentures.

INVESTOR C

32. In or about April and May 2010, Gregg Lorenzo made the following false or misleading statements to Investor C, for which there was no reasonable basis. He told Investor C that:

(a) If he invested in the Debentures, Investor C was guaranteed to get the principal invested in the Debentures back plus interest after one year; and

(b) W2E would be doing very well in a year, at which point Investor C would have the option to convert the Debentures into W2E stock.

33. After speaking to Gregg Lorenzo, Investor C invested a total of $125,000 in the Debentures: $25,000 on April 1, 2010 and $100,000 on May 12, 2010.

F. THE FRAUDULENT E-MAILS TO INVESTORS

34. As stated in paragraphs 18-19 above, on October 1, 2009, W2E filed an amended Form 8-K and its Form 10-Q for the period ended June 30, 2009. Those filings stated that W2E had written off almost all of its previously-reported assets (totaling approximately $14 million) as of June 30, 2009, consisting primarily of $11 million in "intangibles" and "goodwill."

35. On October 1 and the morning of October 2, Frank Lorenzo notified Charles Vista's brokers (including Gregg Lorenzo) by email of W2E's October 1, 2009 filings and included links in his email to the W2E filings on the SEC's website.

36. On October 2, 2009, Frank Lorenzo's assistant, acting on behalf of, and at the direction of, either Frank Lorenzo or Gregg Lorenzo, or both, sent emails to Investor B and another Charles Vista client with the subject-heading "W2E Debenture Deal Points." The emails, designed to solicit those clients' investments in the Debentures, purported to "summarize several key points of the Waste2Energy Holdings, Inc. Debenture Offering," and contained the following false and/or misleading statements concerning W2E:

There are 3 layers of protection:

(I) The Company has over $10 mm in confirmed assets

(II) The Company has purchase orders and LOI's [letters of intent] for over $43 mm in orders

(III) Charles Vista has agreed to raise additional monies to repay these Debenture holders (if necessary)

37. The first statement was false because, by October 1, 2009, W2E had written off nearly all of its assets, and had no "$10 mm in confirmed assets."

38. The second statement was misleading because, as of October 1, 2009, W2E had only a single, non-binding, letter of intent for $43 million and negligible "purchase orders."

39. The third statement was misleading because, when it was made, it was far from certain that W2E could sell the full $15 million in Debentures it was offering, much less "raise additional monies to repay [those] Debenture holders."

40. At the time that Frank and/or Gregg Lorenzo caused Charles Vista to send the October 2, 2009 emails to potential W2E investors, they each knew, or recklessly disregarded, that the statements excerpted in paragraph 36 above were false and/or misleading statements about W2E.

41. On October 5, 2009, Frank Lorenzo and Gregg Lorenzo received an email authored by the Chief Financial Officer of W2E, Craig Brown, which expressly informed them of the "write-off of all of [W2E's] intangible assets . . . of about $11 million."

42. On October 14, 2009, Frank Lorenzo sent two additional emails to Charles Vista customers that contained the very same false and misleading statements that were in the October 2, 2009 emails.

Frank Lorenzo sent the October 14 emails to solicit investments in the Debentures.

43. At the time Frank Lorenzo sent the October 14 emails, he knew, or recklessly disregarded, that the statements contained in those emails about W2E were false and/or misleading.

44. At least one of the recipients of Frank Lorenzo's October 14, 2009 emails invested in the Debentures after receiving the email.

VIOLATIONS

1. As a result of the conduct described above, Gregg Lorenzo, Frank Lorenzo, and Charles Vista willfully violated Section 17(a) of the Securities Act, which makes it unlawful for any person in the offer or sale of any securities, directly or indirectly, to employ any device, scheme, or artifice to defraud, or to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, or to engage in any transaction, practice, or course of business which operators or would operate as a fraud or deceit upon the purchaser.

2. As a result of the conduct described above, Gregg Lorenzo, Frank Lorenzo, and Charles Vista willfully violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, which make it unlawful for any person, directly or indirectly, to employ any device, scheme, or artifice to defraud, to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances

under which they were made, not misleading, or to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

3. As a result of the conduct described above, Charles Vista violated Section 15(c)(1) of the Exchange Act, which prohibits a broker or dealer from effecting any transaction in, or inducing or attempting to induce the purchase or sale of, any security by means of any manipulative, deceptive, or other fraudulent device or contrivance, defined in Rule 15c1-2 to include any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, and Rule 10b-3(a), which makes it unlawful for any broker or dealer, directly or indirectly, to use or employ, in connection with the purchase or sale of any security, any act, practice, or course of business defined by the Commission to be included within the term "manipulative, deceptive, or other fraudulent device or contrivance," as such term is used in Section 15(c) of the Exchange Act.

III.

In view of the allegations made by the Division of Enforcement, the Commission deems it necessary and appropriate in the public interest that public administrative and cease-and-desist proceedings be instituted to determine:

A. Whether the allegations set forth in Section II hereof are true and, in connection therewith, to afford Respondents an opportunity to establish any defenses to such allegations;

B. What, if any, remedial action is appropriate in the public interest against Respondents pursuant to Section 15(b) of the Exchange Act including, but not limited to, disgorgement and civil penalties pursuant to Section 8A of the Securities Act and Sections 21B and 21C of the Exchange Act;

C. Whether, pursuant to Section 8A of the Securities Act and Section 21C of the Exchange Act, Respondents Gregg Lorenzo, Frank Lorenzo and Charles Vista should be ordered to cease and desist from committing or causing violations of and any future violations of Section 17(a) of the Securities Act, and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder; whether, pursuant to Section 21C of the Exchange Act, Respondent Charles Vista should be ordered to cease and desist from committing or causing violations of and any future violations of Section 15(c) of the Securities Exchange Act and Rule 10b-3 thereunder; whether Respondents should be ordered to pay a civil penalty pursuant to Section 8A(g) of the Securities Act, Section 21B(a) of the Exchange Act; and whether Respondents should be ordered to pay disgorgement pursuant to Section 8A(e) of the Securities Act, Sections 21B(e) and 21C(e) of the Exchange Act.

IV.

IT IS ORDERED that a public hearing for the purpose of taking evidence on the questions set forth in Section III hereof shall be convened not earlier than 30 days and not later than 60 days from service of this Order at a time and place to be fixed, and before an Administrative Law Judge to be designated by further

order as provided by Rule 110 of the Commission's Rules of Practice, 17 C.F.R. § 201.110.

IT IS FURTHER ORDERED that Respondents shall file an Answer to the allegations contained in this Order within twenty (20) days after service of this Order, as provided by Rule 220 of the Commission's Rules of Practice, 17 C.F.R. § 201.220.

If a Respondent fails to file the directed answer, or fails to appear at a hearing after being duly notified, the Respondent may be deemed in default and the proceedings may be determined against him or it upon consideration of this Order, the allegations of which may be deemed to be true as provided by Rules 155(a), 220(f), 221(f) and 310 of the Commission's Rules of Practice, 17 C.F.R. §§ 201.155(a), 201.220(f), 201.221(f) and 201.310.

This Order shall be served forthwith upon Respondents personally or by certified mail.

IT IS FURTHER ORDERED that the Administrative Law Judge shall issue an initial decision no later than 300 days from the date of service of this Order, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice, 17 C.F.R. § 201.360(a)(2).

In the absence of an appropriate waiver, no officer or employee of the Commission engaged in the performance of investigative or prosecuting functions in this or any factually related proceeding will be permitted to participate or advise in the decision of this matter, except as witness or counsel in proceedings held pursuant to notice. Since this proceeding is not "rule making" within the meaning of Section 551 of the

Administrative Procedure Act, it is not deemed subject to the provisions of Section 553 delaying the effective date of any final Commission action.

By the Commission.

Elizabeth M. Murphy
Secretary

UNITED STATES OF AMERICA
SECURITIES AND EXCHANGE COMMISSION

Administrative Proceeding File No. 3-15211

In the Matter of GREGG C. LORENZO, FRANCIS V. LORENZO, and CHARLES VISTA, LLC, Respondents.	))))))

26 Federal Plaza
Courtroom 238
New York, New York

September 18, 2013
10:15 a.m.

BEFORE: CAROL FOX FOELAK,
Administrative Law Judge

* * *

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* * *

now that I didn't know." That is their case. "I can't say now that I didn't know." Well, that is not preponderance of the evidence.

So I think in a case like this -- and I am not minimizing this case because the repercussions are tremendous -- I think a couple character witnesses, two would be fine, to give your Honor an idea that you are not dealing with some kind of a Boesky or Madoff. This

is like unbelievable to tell you the truth. I have clients who lost millions of dollars and the

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Proceedings

people who absconded with their money, nothing happened to them.

JUDGE FOELAK: So you are down to two character witnesses that are hopefully going to come in. And the Division -- all they are going to do is testify that they have known him for a certain period of time and had some kind of business with him or didn't have some kind of business with him and always found him --

MR. HANTMAN: That's right.

JUDGE FOELAK: And the Division is going to be able to at least speak to them over the phone ahead of time?

MR. HANTMAN: Exactly, but I am not sure they can come in. The alternative, if they can't -- we prefer they come in, too. But if they can't come in on such short notice we would ask --

JUDGE FOELAK: Let's see if they can't come in.

MR. HANTMAN: Fair enough.

JUDGE FOELAK: Is there anything else?

MR. JANGHORBANI: No. Preserving our objection, your Honor, I think all that needs to

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be said about this has been said.

JUDGE FOELAK: Okay. Please proceed, then.

MR. JANGHORBANI: Good morning again, your Honor.

This is a straightforward fraud case. On October 14, 2009, the respondent, Mr. Frank Lorenzo, made blatant false statements in two e-mails to prospective investors and he did it to sell them debt securities of a start-up tech company called Waste Energy Holdings, Inc.

Now, in October 2009, Mr. Lorenzo was the director of investment banking at Charles Vista. That was Waste2Energy's investment bank. His job as head of investment banking was to understand Waste2Energy's business and financial condition and to help the company raise capital, to help it raise money by selling securities, by offering securities.

Waste2Energy's debt securities were highly speculative. They involved a high degree of risk. Mr. Lorenzo knew that. But to convince these two investors that Waste2Energy's securities were actually safe, he lied about

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fundamental aspects of the company's business and about the debt offering.

So, on October 14, 2009, he sent the following e-mail, this e-mail to two investors. He did it, as he said, to summarize several key points of the Waste2Energy

Holdings debenture offerings. Debentures were the type of debt security here.

Then he said – he described the offering generally and said there are three layers of protection. In other words, investors didn't need to worry about risk so much, they didn't need to worry so much about getting their money back because their investment was protected in these three ways.

First, he wrote, the company had over $10 million in confirmed assets. Second, the e-mail said that the company had purchase orders and letters of intent, LOI's, for over $43 million in orders. Finally, the e-mail said that Charles Vista has agreed to raise additional monies to repay these debenture holders if necessary.

Now, Mr. Lorenzo knew that each of

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these statements was false. He has admitted in testimony under subpoena and under oath that Waste2Energy had far less than $10 million in assets on October 14, 2009. In fact, it had less than a million.

He's admitted that Waste2Energy had virtually no orders and that Waste2Energy was already millions of dollars in debt. And he'd admitted that there was no basis to say that Charles Vista would or even could raise additional money to pay back debenture holders in the event of default.

And he has to admit those things because the circumstantial evidence in this case, Waste2Energy's public filings, the e-mail that Mr. Lorenzo sent and

received, they all show the same thing. They all show that these statements are false and that Mr. Lorenzo knew that well before October 14th.

But he sent his two e-mails anyway and he did it because Charles Vista was paid 20 percent of all of the money that Waste2Energy raised selling debentures and Mr. Lorenzo was hoping to get a cut of that.

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Now, this first layer of protection, there is no question Mr. Lorenzo knew Waste2Energy had nowhere near $10 million on October 14th. He has admitted it in testimony and the documents show it. They show Waste2Energy told Mr. Lorenzo twice before that date that the assets didn't exist. On October 1st, Waste2Energy issued two public files with audited financial statements. Those filings announced a write-off of nearly all the company's assets, over $11 million. And the filings also announced that Waste2Energy had less than 400,000 in total assets as of March 31, 2009.

Mr. Lorenzo received and read those filings two weeks before he sent his e-mail.

And then again on October 5th, ten days before he sent his false e-mails, Waste2Energy's chief financial officer told Mr. Lorenzo again, this time in an e-mail, that Waste2Energy had written off virtually all of its assets.

Mr. Lorenzo has admitted receiving that e-mail, reading it and understanding its

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import. So he actually knew that the company had nowhere near these assets on October 14th.

So where did he get this 10 million number from? He lifted it from an old filing. He took it from Waste2Energy's unaudited financial statements that were prepared as of December 31, 2008. So by October 2009, that number was nearly a year out of date and Mr. Lorenzo knew it had never been confirmed by any auditor. And in fact, as we will see from the e-mails, Waste2Energy repeatedly, over the summer and early fall of 2009, refused to confirm for Mr. Lorenzo that that asset still existed.

So even before the October 1st write-off, even before the October 14th e-mail, Mr. Lorenzo knew he had no business saying that this asset had been confirmed by anybody.

But it is a little academic because there is no question that he actually knew the asset didn't even exist on October 14th.

His second layer of protection. He wrote that the company has purchase orders and letters of intent for over 43 million in orders.

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Well, that makes it sound like Waste2Energy has millions of dollars in contracts. In other words, your investment is protected by Waste2Energy's thriving business, by its sales, multiple purchase orders and multiple letters of intent. But that was false and Mr.

Lorenzo knew it. He knew that Waste2Energy had very few actual orders in October 2009.

This 43 million number, he based this entirely on a single non-binding letter of intent for a potential purchaser in the Caribbean. In other words, one customer's non-binding agreement simply to think about buying Waste2Energy's products. Certainly not multiple orders and the multiple LOIs that he promised investors. And just as certainly it provided no protection to debenture investors.

There is no assets, no orders, no sales. Mr. Lorenzo knew it. But he had a third layer of protection. He wrote that Charles Vista has agreed to raise additional money to repay these debenture holders if necessary.

In other words, "Don't worry. Even if your investment is not protected by millions in

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assets and millions in orders, Charles Vista's got your back. We will raise the additional money to make sure you don't lose anything." But Mr. Lorenzo had no basis to say that.

He knew that this layer was at best misleading. He's admitted to that. There was no agreement between Charles Vista and Waste2Energy to raise additional money for the purpose of paying back debenture holders in event of default. Mr. Lorenzo has admitted he didn't even believe his statement at the time he made it. That he didn't believe that, even if it wanted to, Charles Vista would be able to find enough additional buyers to repay debenture holders. And that

was because Waste2Energy had already raised too much debt.

In fact, 70 percent of all the money Charles Vista managed -- Charles Vista was also a broker-dealer, and 70 percent of all the money it managed was invested in Waste2Energy. So no reason to think Charles Vista would be able to find additional investors.

And in the end Waste2Energy did default on its debentures and Charles Vista

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didn't raise any money to pay them back. So Mr. Lorenzo made a promise he knew he had no basis for, one that provided no protection.

Frank Lorenzo has no defense to these charges. His answer is simply to try to spread the blame to others. He blames Waste2Energy for not telling him sooner about the write-off but it did, on October 12th and October 5th, weeks before he sent his e-mails.

He said he was checked out at work, that others should have caught his misstatement. That is just nonsense. Mr. Lorenzo was an industry veteran. He was the head of investment banking. It was his job to know about Waste2Energy's financial condition.

And as the e-mails will show, your Honor, and as the testimony will show, Mr. Lorenzo was doing his job during that period. He was following Waste2Energy's financial condition, he was following the status of the audit over the summer and fall of '09 and he was following the disclosure in the company's private placement memorandum.

As I said earlier, he repeatedly asked

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Waste2Energy to confirm the 10 million assets still existed and the company repeatedly refused. He knew exactly what was going on with the company and he can't claim to be in the dark now.

Finally, he blames his colleagues at Charles Vista. He says that other senior management also signed off on the e-mails. But that just completely misses the point because there is no question that Mr. Lorenzo is responsible for his own statements in his own e-mails. And there is no question that he knew those statements were false, but he sent the e-mails anyway.

And at least one of the recipients, a man named Vishal Goolcharan, went ahead and invested $15,000 in Waste2Energy's debentures.

The other investor he solicited, a man named William Rothe, he didn't invest, that is true, but that doesn't excuse Frank Lorenzo's false statements. It is unlawful to make a false statement simply while offering securities. It is of no moment that Mr. Rothe didn't invest. In fact, Mr. Lorenzo certainly

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hoped he would invest. He was trying to convince him to buy. That is the entire purpose of this e-mail.

He sent the e-mails, your Honor, he sent them in the hope of making money. As I mention earlier, Charles Vista got about 20 percent of all of the debenture money raised. And Charles Vista's owner

had promised Mr. Lorenzo a cut of any debentures that he was able to sell.

So, he went ahead, he sent e-mails he knew to be false. That is what the evidence at this hearing will show. As a result of Mr. Lorenzo's blatant false statements in these two e-mails, he violated Section 17(a) of the Securities Act, Section 10(b) and Rule 10(b)(5) of the Exchange Act.

At the end of this trial, your Honor, the Division will ask that this Court find Mr. Lorenzo liable on all counts, that it impose cease and desist orders, that it award civil money penalties and that it implement all relevant statutory bars.

Thank you, your Honor.

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MR. HANTMAN: Your Honor, a very good opening statement and clearly it was probably prepared to be used against Gregg Lorenzo, who is the owner of Charles Vista, whom the bulk of the government's case was against Charles Vista and Gregg Lorenzo.

Now having reached some kind of resolution with him, apparently they have just taken what clearly and likely is true and applies to Gregg Lorenzo and they are trying to use what they have for Francis Lorenzo.

I am not going to rely on rhetoric. Obviously, anything I say or SEC counsel says is not evidence. The only evidence is what your Honor hears by witnesses under oath or documents that are submitted and

approved by this Court. So I think my letter of September 16, 2013, sums up our position. This e-mail really was at the request of Gregg Lorenzo and Spiro. I don't know where they are. They are not here but it was at their request that this was sent.

It wasn't Mr. Francis Lorenzo's desire to send this stuff out. He didn't even know these gentlemen. They would have no reason to

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even know who he is. I think the evidence will show he never spoke to these gentlemen. They would have absolutely no reason in the world to rely upon anything that he would send them or his secretary would send them.

I could go on and on but I don't think it is appropriate. We will rely upon the evidence or what we think is lack of evidence. Again, these are a lot of statements that the government has made and naturally, having made what they say are unequivocal admissions, which we claim are not admissions at all, we leave them to their proof by a preponderance of the evidence that they can sustain their burden on all the elements: Of the scienter, of the proximate cause and of the losses. On all three they have to substantiate beyond a preponderance of the evidence.

Plus, I think W2Energy, to claim that they told Mr. Lorenzo this and told him that and everything else and that he understood what they told him I think is conjecture. But we'll hear what the evidence proves.

Thank you, your Honor.

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JUDGE FOELAK: Okay.

MR. KAUFMAN: Morning, your Honor. Jack Kaufman for the Division. The Division calls Craig Brown.

JUDGE FOELAK: Mr. Brown, before you sit down I will put you under oath.

Whereupon,

CRAIG BROWN,

having been first duly sworn/affirmed, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. KAUFMAN:

Q. Morning, Mr. Brown.

A. Good morning.

Q. Could you state and spell your full name for the record?

A. Craig, C-R-A-I-G, Littleton, L-I-T-T-L-E-T-O-N, Brown, B-R-O-W-N.

Q. How old are you, sir?

A. 46.

Q. How are you currently employed?

A. I work for the Gwinnett County Chamber of Commerce in Duluth, Georgia as the CFO.

Q. What do you do for them?

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A. CFO.

Q. Chief financial officer?

A. Chief financial officer.

Q. In 2009, how were you employed?

A. I was employed by Waste Energy Holdings starting in July 2009 as chief financial officer.

Q. How long did you remain as chief financial officer of Waste Energy Holdings?

A. Through February 2011.

Q. What were your duties generally speaking as CFO of Waste Energy?

A. Initially when I joined the company my duties were to assist the company get caught up and current on its filings with the SEC, so it would have involved accounting, financial reporting, some work with financing of the company. But principally, for the time I was there, the first six months anyway, it was a lot of financial reporting responsibilities.

Q. Did those responsibilities change after the first six months you were at Waste2Energy in any way?

A. Not dramatically, no.

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Q. How long did you stay as CFO at Waste2Energy?

A. I resigned February 2011.

Q. While you were at Waste2Energy, was there someone you reported to?

A. Yes.

Q. Who was that?

A. Peter Bohan, who was the CEO.

Q. Chief executive officer?

A. Correct.

Q. Can you describe, please, Waste2Energy's financial condition when you began as chief financial officer?

A. It was very, very poor.

Q. Can you elaborate a little on that? What do you mean by that?

A. They were very low on cash in the business, they had a lot of outstanding payables to service providers and vendors, some of which put the company in a position where they were unable to remain current on their filings. And some of that triggered some of the delays we had actually in connection with the work completed.

Q. During the time period you were there,

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what happened to the financial condition? Did it improve, stay the same, get worse --

A. It got worse.

Q. I should ask you, what was Waste2Energy? What was the company?

A. It was a small public company -- it was a private company up until May 2009. It went public through a reverse merger and the premise of the business was they had a technology, a gasification technology in which they had the know-how to convert solid waste to gas to form electricity basically?

Q. Were they ever able to do that, convert it to electricity?

A. Yes.

Q. When was that?

A. A project over in the UK in 2009, 2010.

Q. Was that ever converted to electricity, the energy in that project?

A. I don't recall if they ever were officially generating electricity on that site.

Q. And when you left the company in February 2011, how would you describe its

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financial condition?

A. Dire. Very poor.

Q. While you were at Waste2Energy, did the company generate any revenue?

A. Yes.

Q. What source of revenue did it have, or sources?

A. The revenues were contractual revenues for -- there is a couple sources. One was on a project they had in the UK, the principal project they had during my tenure there, a plant called Dargavel.

They had several equipment sales. They had revenue from sales of smaller pieces of equipment and they had fee revenue for basically engineering studies that they would do for prospective customers.

Q. How much of the company's revenue was attributable to the Dargavel contract as opposed to the others?

A. The majority of it. Probably 90-plus percent.

Q. Let me ask you to look at Exhibit 55. There are some binders in front of you. If you

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can find the tab 55? If you have trouble I can show you.

This is a document, the first page says Dargavel energy from waste project. Do you see that, sir?

A. I do.

Q. This is Exhibit 55. Do you recognize this document?

A. Yes.

Q. What is it, sir?

A. This was a contract that had been entered into by the company, subsidiary in the Isle of Man with ASCOT Environmental, the customer for the Dargavel contract.

Q. Is this the Dargavel contract you were just testifying about?

A. Yes.

Q. If you could turn to page 7, the seventh page of the document. They are not numbered. And if you look toward the bottom of the page, the paragraph numbered 3, do you see it says "The contract price is the sum of --" and there is a number and then it is also written 3,286,943 Euros. Do you see that?

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A. Yes, I do.

Q. I take it that was the total contract price in this contract?

A. Right.

MR. KAUFMAN: Your Honor, I have forgotten to offer the document in evidence. We offer it.

MR. HANTMAN: If I can just have some voir dire on this, your Honor.

JUDGE FOELAK: Okay.

VOIR DIRE EXAMINATION

BY MR. HANTMAN:

Q. Were you with the company when this contract was entered into?

A. No, I was not.

Q. Did you participate in any negotiations with respect to this contract?

A. I did not.

Q. Do you know whether this is an aut[illegible] contract? Can you swear under oath that this is a contract that was even signed?

A. The contract was signed based on what I have here.

Q. But you don't have any personal

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knowledge of the circumstances leading up to this contract, do you?

A. I was not there when the contract was executed.

MR. HANTMAN: Your Honor, I would object. This witness isn't competent to –

JUDGE FOELAK: Is it your position this contract is false or didn't exist?

MR. HANTMAN: Well, I don't know that that is my position, but I think whether it gets admitted in evidence is whether it is properly authenticated, if the witness can testify that this is accurate. That is all. I am not suggesting that it is a fake or something.

MR. KAUFMAN: Your Honor, the witness has identified this as the Dargavel contract. It is a business record that was part of the company's records.

JUDGE FOELAK: Very well. The Exhibit 55 is admitted.

MR. HANTMAN: Under the business records, I would have no objection, your Honor.

(So received in evidence as Division Exhibit 55.)

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CONTINUED DIRECT EXAMINATION

BY MR. KAUFMAN:

Q. Looking back at page 7, I wanted to ask one more question about the price. Did that price ever change while you were the CFO of Waste2Energy?

A. The contractual price never changed.

Q. Was the contract ever profitable, the ASCOT contract we are talking about?

A. No, it was not.

Q. As of September 2009, was Waste2Energy actually due any money under this contract?

A. Restate that? As of what period?

Q. As of September 2009. By that time?

A. I have to go back and look at what we were carrying on the balance sheet. I don't recall.

Q. Okay.

A. The contract at that point had incurred some cost overruns.

Q. Let me direct your attention to tab 46, sir. Let me know when you have that in front of you, please.

A. Okay.

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Q. Sir, do you recognize that document?

A. Yes.

Q. It is titled Form 10-Q, Waste2Energy for quarterly period ending September 30, 2009. Do you see that?

A. Yes.

Q. Could you turn to the very last page. You see there is a signature block there?

A. Yes.

Q. Then there is a date. Do you understand what that signature block signifies?

A. Yes.

Q. What is that?

A. That is the signers and the date on which the document is filed with the Commission.

Q. You were one of the people who signed this document?

A. Yes.

Q. And caused it to be filed with the SEC?

A. Correct.

MR. KAUFMAN: The Division offers Exhibit 46.

MR. HANTMAN: No objection, your

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Honor.

JUDGE FOELAK: Exhibit 46 is admitted.

(So received in evidence as Division Exhibit 46.)

Q. What is Exhibit 46, just briefly, Mr. Brown?

A. It is a quarterly report that is required to be filed by public companies with the Securities and Exchange Commission.

Q. Was this for a particular period of time?

A. Yes. This was for the three-month period ending September 30, 2009.

Q. And it was filed in November, is that right, 2009?

A. Filed November 16, 2009.

Q. Please turn to page 13? By that number I mean on the upper right-hand corner. You will see page 13 of 36.

We are also putting it up on the screen if that is easier for you.

I will ask you to look at what is called note 4. It says, "Contracts in progress." There are some numbers there. I am

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going to ask you, does this help you to determine whether any revenues were still actually owed

Waste2Energy as of that time, September 30, 2009, on the Dargavel contract?

A. Well, at this time there was already a loss that had been incurred on the contract so, no, I don't believe there were.

Q. You don't believe there were additional revenues that were going to come in on this contract as of that date. Is that what you are saying?

A. That's correct, as we had highlighted in the footnote there were ongoing discussions between the client and the company, Waste2Energy, as to the treatment of those costs.

Q. Just to be clear, the contract being discussed in this note, is that the Dargavel contract, the ASCOT contract you have been talking about?

A. Yes, it is.

Q. It says, if you look at the second sentence of the full paragraph that starts "Estimated" it says "The one contract in

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progress has incurred cost overruns and other costs." Do you see that?

A. Yes.

Q. And that is referring to the Dargavel contract?

A. Yes.

Q. Is it fair to say there were no other contracts in progress with respect to Waste2Energy at the time?

A. Correct.

Q. Was Waste2Energy -- you can take that off the screen.

Was Waste2Energy due any other monies under any other contracts as of this time, September 30, 2009?

A. No major construction contracts, no.

Q. Well, was it due any money at all?

A. I don't recall if there was any pending small equipment sales. But, no -- there -- there would have been nothing else.

Q. Nothing else?

A. According to the balance sheet.

Q. You mentioned before that there were some other contracts other than Dargavel while

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you were at Waste2Energy. Isn't that right?

A. Yes, but not of that magnitude.

Q. What was the total amount of those other contracts while you were at Waste2Energy?

A. If you were to aggregate a couple of smaller equipment sale contracts as well as some of the design studies that were entered into, I would guess --

Q. We don't want you to guess, sir. What is your best recollection?

A. Less than $500,000.

Q. Okay.

A. In the aggregate, during my tenure.

Q. Are you familiar with something called a letter of intent or LOI?

A. Yes.

Q. What do you understand that to be?

A. It's an agreement between two parties that are evaluating entering into a more formal contractual arrangement. It basically defines the scope of what those preliminary terms may look like.

Q. In your understanding, does it obligate either party to do anything, this LOI?

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A. No.

Q. No?

A. No.

Q. Did Waste2Energy have any letters of intent or enter into any letters of intent, let's say, as of October 2009?

A. No.

Q. Not at all?

A. Not as of October 2009.

Q. Let me ask you to look at Exhibit 15, tab 15?

A. 50?

Q. 15.

Do you have that in front of you, sir?

A. Yes.

Q. Do you recognize that document, titled "Maven Media Holdings, Form 8-K, date of report May 2009."

Do you recognize that document?

A. I do.

Q. What is that?

A. This was the filing that was made with the Securities and Exchange Commission at the time the company entered into the reverse merger

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and a subsequent equity offering tied to the merger.

MR. KAUFMAN: The Division offers Exhibit 15.

JUDGE FOELAK: Hearing no objection, Exhibit 15 is admitted.

(So received in evidence as Division Exhibit 15.)

Q. Mr. Brown, did you have any involvement in preparing this document?

A. No, I did not.

Q. Was this prepared prior to your being at Waste2Energy?

A. Yes.

Q. Do you know who prepared it?

A. It would have involved management of the company but I think largely it was a firm called Citrin Cooperman did a lot of the work.

Q. And who were they?

A. They were an accounting firm that had a unit that did a lot of financial reporting work for small public companies.

Q. Just to be clear, what was Maven Media Holdings?

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A. Maven Media was the name of the company, the shell company that was purchased and ultimately the name was changed to Waste Energy Holdings.

Q. That is the former name of Waste2Energy Holdings?

A. Yes. Correct.

Q. If you could turn to page 15, again the upper right-hand corner page numbers? We'll put it up on the screen.

I am sorry. I gave you the wrong page number. Page 63, Exhibit 15.

This page is titled "Waste2Energy Inc. and subsidiaries balance sheet."

Do you have that in front of you?

A. I do.

Q. What is this showing generally?

A. This is showing the financial position of Waste2Energy as of December 31, 2008 based on unaudited financial statements as of that period.

Q. What does that mean, "unaudited financial statement"? What does the term "unaudited" mean?

[p.56]

A. It was an interim period. The company had a fiscal year end of March 31st and they had not been subject to a full external audit by an outside accounting firm.

Q. And is there any significance to the fact it was unaudited?

A. No. It is not uncommon to file unaudited statements in these type of filings.

Q. If you could look at the line that says "Total assets," it says "$13,987,764." Do you see that?

A. Yes.

Q. Is it fair to say that that was the recorded unaudited number for the total assets of Waste2Energy as of December 31, 2008?

A. That's correct.

Q. If you could look up a few lines, there is a line that says "Intangibles, net, $10,038,558." Do you see that?

A. Yes.

Q. Do you know what that intangibles net was?

A. That was -- the bulk of that was the value that was assigned to the technology and

[p.57]

the know-how, I guess, that was acquired that was the basis of, the foundation of this company.

Q. Okay.

A. They made a couple different acquisitions and that was the calculated value by a third-party appraiser.

Q. And the goodwill line below that, $470,274, what was that?

A. That, if I recall, was the value that was assigned to the workforce, the people that were initially in Iceland that were behind the development of the technology.

Q. This Form 8-K, when was it filed?

A. May 28, 2009.

Q. Let me ask you to just turn to I think it is two pages earlier, page 61. There is a date there, June 3, 2009. What does that tell you?

A. That was actually the filing date. June 3rd.

Q. 2009?

A. 2009.

Q. Did there come a time when

[p.58]

Waste2Energy publicly reported -- when its publicly reported assets changed significantly?

A. Yes.

Q. When did that happen?

A. There was an amended 8-K filed, an amendment of the document we were just reviewing, on or around the 1st of October 2009.

Q. October 1, 2009? Is that right?

A. Yes.

Q. And were you personally involved in preparing the amended 8-K filing?

A. I was.

Q. Was there any other public filing filed on October 1, 2009 for Waste2Energy?

A. Yes.

Q. What was that?

A. There was a quarterly report for the quarter ended June 30, 2009 filed.

Q. Is that also known as a Form 10-Q?

A. Yes.

Q. What was your -- were you involved in the preparation of that as well?

A. Yes.

Q. What was your involvement in the

[p.59]

preparation of the amended 8-K and the Form 10-Q?

A. A lot of my involvement on the 8-K was surrounding working with the audit form and third-party accountants and management to get a handle on the evaluation of those intangibles that were on the balance sheet, the $10 million number.

Q. And who were the auditors you worked with?

A. The third-party auditor was a firm called Marcum.

Q. Marcum? How do you spell that?

A. M-A-R-C-U-M.

Q. Did you work with anyone else other than Marcum?

A. That was audit firm and we also worked with Citrin Cooperman who had been involved in the initial preparation of the financial statements that were filed in May or June 3rd.

Q. Were there any attorneys involved?

A. Yes.

Q. Who were they?

A. Sichenzia Ross Friedman.

[p.60]

Q. When did you have discussions with the auditors about this audit? When did that take place?

A. Probably my first week on the job. So, first -- early July is when I first started having dialogue with them.

Q. Did you continue to have those discussions through the end of September 2009?

A. I did.

Q. What happened -- you said you were looking at the intellectual property. What ultimately ended up happening with that report of the intellectual property?

A. It was totally written off. It was deemed to be totally impaired and the value of that was written down to zero.

Q. You mean the value of the $10 million intellectual property was written down to zero?

A. Yes, as well as the goodwill line item.

Q. Let me ask you to turn to tab 30?

MR. HANTMAN: Excuse me. Was there a date this was done?

Q. Were you talking about the October 1st

[p.61]

filing, sir, when you said it was written down to zero?

A. Yes. When the -- audited statements for 3/31/2009 were completed that was filed on October 1st.

Q. Could you, please, turn to tab 30. Division Exhibit 30 appears to be a series of e-mails to and from Craig Brown. I am going to ask you, sir, if you sent and received these e-mails?

A. Yes, I did.

Q. It looks like they were all on August 19, 2009.

The Division offers Exhibit 30.

JUDGE FOELAK: Hearing no objection, Exhibit 30 is admitted.

(So received in evidence as Division Exhibit 30.)

Q. I want to start with the second page of this e-mail chain. The first in time appears to be from a David Manno to C. Brown and it is on August 19th. Do you know who Mr. Manno is?

A. Yes, I do.

Q. Who is that?

[p.62]

A. He was an attorney with Sichenzia Ross Friedman.

Q. Was he involved in working on this audit?

A. Yes.

Q. And it is to C. Brown. Is that to you?

A. That was my e-mail address, yes.

Q. In the text of the e-mail it says, second sentence begins, "Because the 10-Q was not filed today, the bulletin board will assign an E to the company's symbol" then there is a parenthetical. The next sentence says "If the company does not file the 10-Q within 30 days of tomorrow, it will be delisted."

Is that 10-Q the one you have been talking about that was ultimately filed on October 1st?

A. Yes, it was.

Q. Now going to the next e-mail in line, you can see it starts at the bottom of the first page and then goes to the second page. This one is from a Thomas Rose to you, Mr. Brown. Is that correct?

[p.63]

A. That's correct.

Q. Who is Mr. Rose?

A. Tom was another attorney at Sichenzia Ross.

Q. It looks as though he is responding to the earlier e-mail and he said – he says, "What can we do to get the Q filed? I don't see how CV can sell anything when the company isn't current on its filings. Are they aware if this is coming?"

Do you see that?

A. I do.

Q. Again, do you understand the Q he is referring to there to be the 10-Q you have been talking about?

A. Yes.

Q. It says "I don't see how CV." Do you understand what CV is referring to?

A. Yes. Referring to Charles Vista.

Q. Who is Charles Vista?

A. That was the name of the investment banking firm that had been working with the company to help raise money for the company's financing.

[p.64]

Q. Do you understand what he means when he says "I don't see how CV can sell anything when the company isn't current on its filings"?

A. Yes.

Q. What does that mean to you?

A. He doesn't see how they can market if the company was not current in its filings with the Securities and Exchange Commission and was potentially on the brink of being delisted.

Q. Market what?

A. Sorry?

Q. You said market.

A. Market, sell securities.

Q. To raise money --

A. Market securities to raise money for Waste2Energy.

Q. Then the next e-mail in the chain appears to be from you later that day. Is it fair to say this is your response to those e-mails?

A. Yes.

Q. You say, "We are continuing to work --" second sentence. "We are continuing to work on 3/31 numbers and hope to get the audit

[p.65]

going this week and be in a position to file audited statements for March 31st in the next two weeks. We expect to be able to get a 10-Q done and filed in short order after the 3/31 numbers are filed with the SEC." Do you see that?

A. I do.

Q. Again you are talking about this same 10-Q that eventually got filed on October 1st. Is that right?

A. That's correct.

Q. Then the next e-mail, it looks as though you forwarded it -- you forwarded this chain to Francis Lorenzo. Is that correct?

A. Yes.

Q. And you say "FYI." Why did you forward it to Francis Lorenzo?

A. I wanted to make sure they were in the loop in terms of the fact that we were working on the filings, both the audited statements which needed to be filed before the Q got filed.

But there was a timeline that we had in mind as to when we could have that completed. I just wanted them to be current in terms of

[p.66]

where we stood.

Q. Who is Francis Lorenzo and what did he have to do with this?

A. Mr. Lorenzo was an investment banker with Charles Vista.

Q. And was there a particular reason you sent him these e-mails?

A. He and Mr. Lorenzo, Gregg Lorenzo, were the two individuals at Charles Vista who had the major interaction with our company.

Q. With Waste2Energy?

A. With Waste Energy Holdings, yes.

Q. Interaction in terms of what?

A. Just being the point persons in terms of conversations. They were the primary points of contact between Waste2Energy and Charles Vista.

Q. For what purpose?

A. For working on proposed financing transactions for the company.

Q. Okay. And then you see Mr. Lorenzo's response, "Thanks for the update and the great work." Do you see that?

A. I do.

[p.67]

Q. Did you ever meet Frank Lorenzo in person?

A. No.

Q. You did not. Okay.

Let me ask you now to turn to tab 22. I ask you to take a look at it. It is -- it says "Form 10-Q for the quarterly period ended June 30, 2009."

Do you recognize this document?

A. Yes.

Q. What is it?

A. It is the filing that we have been discussing for the three-month period ending June 30, 2009.

Q. If you could turn to the last page, please? You should see a signature page.

A. Yes.

Q. There is a date. Can you explain what these signatures are and what that date mean?

A. The filing was signed by Peter Bohan, the CEO, and myself the CFO. And it was filed October 1, 2009 with the Securities and Exchange Commission.

Q. If you could turn --

[p.68]

MR. KAUFMAN: Oh, the Division offers Exhibit 22.

JUDGE FOELAK: Hearing no objection, Exhibit 22 is admitted.

(So received in evidence as Division Exhibit 22.)

Q. If you could, please, turn to page 4 of this document? This page is titled "Consolidated financial statements and notes to the financial statements, Waste2Energy Holdings, Inc.," et cetera.

Can you tell us generally what this page is showing?

A. It is showing the financial position of Waste2Energy for the quarter ended June 30, 2009 and a comparison of that position with the final audited numbers for the year ended March 31, 2009.

Q. So on the right-hand side, the left column is unaudited numbers and the right column are audited?

A. Yes, that's correct.

Q. Can you just, very briefly, what is the difference between an audited financial

[p.69]

statement and unaudited? Can you explain that?

A. An audited statement has been through a pretty rigorous examination by a third-party audit firm who has tested and validated the transactions or a sample of the transactions and issued an opinion as to the accuracy of those numbers.

Q. And unaudited has not been through that process?

A. Yes. They typically do a review but it's not subject to an audit opinion or subject to a full audit.

Q. There is an assets line for both the June 30th quarter and March 31st quarter. For June, it says $660,408. Is that correct?

A. Yes.

Q. Looking at the list of assets, there is no longer one for intangibles. Is that correct?

A. That's correct.

Q. And why is that?

A. The value of those intangible assets was written off to zero as part of the year-end 2009 audit.

[p.70]

Q. And there is no line for goodwill there. Is that correct?

A. That's correct.

Q. And why is that?

A. It was also deemed to have zero value.

Q. Could you, please, turn to page 106 of this -- wait a minute. If you can take this one off.

I want to show you Exhibit 16. Exhibit 16 says on the first page "Form 8-K/A Amendment Number 1," and it says "Waste2Energy Holdings, Inc."

Do you see that?

A. I do.

Q. Do you know what this document is?

A. This was the document that was filed to update the initial 8-K from June 3rd but to include a fully audited set of financial statements for the period ending March 31, 2009.

Q. And did you play a role in preparing this? I think you testified before.

A. Yes, I did.

Q. If you could turn to page 66, it is another signature page. There is a line for

[p.71]

Craig Brown that says October 1, 2009. Can you explain what those matters mean?

A. Yes. That was the date on which this document was filed, and I was the individual that signed the document on behalf of Waste2Energy.

MR. KAUFMAN: The Division offers Exhibit 16.

JUDGE FOELAK: Hearing no objection, Exhibit 16 is admitted.

(So received in evidence as Division Exhibit 16.)

Q. Please turn to page 69 of Exhibit 16. Do you have that in front of you, sir?

A. I do.

Q. It says "Waste2Energy Inc." and "Subsidiaries consolidated balance sheets." Can you tell us what this page shows generally?

A. Yes. This is basically two fully audited periods. The audited period dated March 31, 2009 compared to what the audited period dated March 31, 2008.

Q. The March 31, 2009 numbers, are these the same as we saw just now in the October 1st

[p.72]

filed 10-Q?

A. Yes, they are.

Q. And again there is no listing for intangibles. Is that correct?

A. Correct.

Q. And the reason for that is the same reason you gave before with respect to the 10-Q?

A. That's correct.

Q. And again there is no goodwill listed. Is that correct?

A. That's correct.

Q. And is your answer as to why that isn't there the same as to why it is not on the 10-Q?

A. Yes, it is.

Q. Could you, please, turn to page 106 now of this document? This page is titled "Note 7, goodwill and technology." Do you have that in front of you, sir?

A. I do.

Q. Generally speaking, what is this note describing?

A. This basically is a summary of the assets that were on the books at a gross amount

[p.73]

adjusted for currency and other things that would affect the U.S. reporting value of those amounts.

Also the key line item is that it shows an impairment charge being recorded against the value of those assets to bring it down to a zero value.

Q. Is this a description of what happened with the intangibles and goodwill that we were just talking about?

A. Yes.

Q. We have just looked at a 10-Q and amended 8-K that were filed for Waste2Energy on October 1, 2009. The 10-Q had numbers as of June 30, 2009, correct, on the balance sheet?

A. That's correct.

Q. We can look back at it if you need to.

A. No. That is correct.

Q. When you filed these documents were you aware of any material change between June 30, 2009 and October 1, 2009 to the balance sheet?

A. Between June 30th, from a date standpoint?

[p.74]

Q. Right.

A. I mean, when I joined the company in July we had not yet filed either the audited 3/31 or the June -- I am not sure I understand the question.

Q. If it doesn't make sense to you that is fine. What I am asking is, they were filed October 1, 2009 but the financial statements were as of June 30th. Is that correct?

A. Right.

Q. When you filed them, were you aware of any material change between June 30th and October 1st?

A. No. No material changes.

Q. Let me ask you to turn to Exhibit 19. Exhibit 19 appears to be an e-mail from Craig Brown to several people dated October 5, 2009. Do you see that, sir, in the upper part of the document?

A. Yes, I do.

Q. Then there is text below it. Did you send this e-mail?

A. Yes, I did.

MR. KAUFMAN: The Division offers

[p.75]

Exhibit 19.

JUDGE FOELAK: Hearing no objection, Exhibit 19 is admitted.

(So received in evidence as Division Exhibit 19.)

Q. You will see the subject line says "Re W2E financial filings." Do you see that?

A. Yes.

Q. Below that where the body starts it says, "The accumulated deficit we have reported is due to three primary issues." Do you see that?

A. Yes.

Q. Can you tell us generally what this e-mail is about and why you sent it?

A. Yes. There was a request made from an individual at Charles Vista, Mr. Zdanow, on October 5th asking about -- I guess he was looking at the filings and did not understand why there was an accumulated deficit of 18 million.

Q. You are referring to his e-mail that is part of this document?

A. Yes, an e-mail in this chain which

[p.76]

triggered my response to this e-mail.

Q. Okay.

A. But basically it was to highlight for those individuals copied on the e-mail the key reasons why there was a deficit and why the losses were so significant, which had already been reported in the filings that we had made publicly.

Q. Where did Mr. Zdanow work?

A. He was with Charles Vista.

Q. It looks as though you copied Francis Lorenzo as well. Is that right?

A. I did.

Q. Why did you copy Mr. Lorenzo?

A. Typically Mr. Lorenzo was copied on any of these type of communications, but he was also on the communication that Mr. Zdanow sent over at 2:34 p.m. in which I was copied on this.

Q. I see. So you hit "Reply all," in other words?

A. Yes.

Q. You say he was -- Mr. Frank Lorenzo was typically on these kinds of exchanges. What kind of exchanges do you mean?

[p.77]

E-mail exchanges between Charles Vista staff and Waste2Energy management involving financial questions or issues.

Q. Okay. If you look -- you said there were three primary issues. If you just look at issue number 2, it is the first sentence, that says "Write-off of all our intangible assets that were tied to our purchase of Enerwaste in Europe in 3/31 period of about $11 million." Do you see that?

A. I do.

Q. Is that referring to the write-off you have been talking about that ended up writing off the intangibles that then didn't show up --

A. Yes. That is the write-off referred to.

Q. Can you describe how Waste2Energy was funding its operations as of September 2009?

A. Basically through short-term financing from some bridge loans that had been, I guess, put together issued by Charles Vista with some of their investors.

Q. Okay. And what was Charles Vista's role?

[p.78]

A. Charles Vista was the investment banking firm who marketed the securities.

Q. And how would you describe how that was going, the cash flow of the company and these offerings?

A. Not well.

Q. Could you elaborate on that?

A. There were – going back to the May, June equity raise, that equity raise tied to the initial taking the company public did not go as planned in terms of how much capital they were able to raise through that offering.

That just kind of trickled down through the summer and fall as we had to rely on bridge financings to assist the company to continue to maintain its operation.

Q. By "bridge financings," do you mean debt financings?

A. Yes, short-term debt typically.

Q. Let me ask you to look at Exhibit 7.

Before I do that, can you explain what role the debt financings played and how that affected cash flow of Waste2Energy?

A. Well, it was key because the company

[p.79]

really was not generating cash flow from its operating business at that time. So it was reliant on financing through these debt transactions to generate capital to operate on.

Q. Let's look at Exhibit 7. On the first page it appears to be an e-mail dated September 1, 2009 from Peter Bohan to several individuals including you, Mr. Brown. Is that correct?

A. Yes.

Q. And did you receive this e-mail on September 1, 2009?

A. Yes.

MR. KAUFMAN: The Division offers Exhibit 7.

JUDGE FOELAK: Hearing no objection, Exhibit 7 is admitted.

(So received in evidence as Division Exhibit 7.)

Q. If you could turn to the second page of this exhibit, there is an e-mail at the bottom of the page from Francis Lorenzo to Peter Bohan and you, Mr. Brown. Is that correct?

A. Yes, that's correct.

[p.80]

Q. The subject line says, "Only $90,000 in cash remaining" and this is from Francis Lorenzo.

Do you have an understanding of what that means?

A. Yes. That is a reference to the amount of cash available in the company as of that date as of that request.

Q. As of September 1, 2009?

A. I believe so, yes.

Q. And then Mr. Lorenzo says, "Gentlemen, as previously discussed, please forward me the use of proceeds for the bridge money that was just raised." It looks like 2.5 million. Is that correct?

A. Yes.

Q. Is the bridge money the debt financing or some of it that you were referring to before?

A. It is.

Q. And then there is a response e-mail which is the one we started with from Peter Bohan the same day that you are copied on. Is it fair to say that this is Mr. Bohan's response?

[p.81]

A. Yes.

Q. If you look at the first paragraph, the paragraph numbered 1 of this response, it says, "The bridge would have covered OPEX for four months if we did not have

to incur repayment of notes and significant repayment to accounting, audit and legal firms."

Do you see that?

A. Yes.

Q. Do you know what Mr. Bohan meant by "OPEX"?

A. Operating expenses.

Q. And generally what is your understanding of what Mr. Bohan is saying there?

A. That without having to shift a lot of the money that was raised to basically paying off other notes that had been issued previously to either refinance or pay them off altogether, and pay off some of the accounting and legal firms that were supporting the company through its compliance process, the company would have had money to operate more easily with respect to paying salaries, rents, other operating costs to run the business.

[p.82]

Q. And paragraph number 2 says, "While the bridge raises have helped in the short term, they have created a never-ending demand to replace them with additional notes and very little of this money comes to the company."

Do you see that?

A. Yes.

Q. Do you understand what company Mr. Bohan is referring to?

A. He is referring to Waste2Energy.

Q. Generally what is your understanding of what he was saying there?

A. I think what he was trying to suggest is the company had been put into a cycle where it was faced with not only having cash needs but also facing maturities of other short-term borrowings that had to be paid off and, therefore, very little of the net raise was coming actually back into the company.

Q. Then in the third paragraph, the last couple of lines -- actually the last phrase on the last line. "This is a never-ending loop that only benefits CV in the short term." Do you see that?

[p.83]

A. I do.

Q. "CV" there, is that Charles Vista?

A. Yes.

Q. What is your understanding of what Mr. Bohan is referring to there?

A. I think what he was referring to -- my assumption is that it was referring to the fact that Charles Vista was, for each transaction, earning a commission and able to maintain a flow of revenue into their firm.

Q. Can you turn to the last page of this document? There is an attachment it looks like. It says "uses of proceeds from $1.5 million bridge loan." Do you see that?

A. Yes.

Q. Do you have an understanding of what that attachment, generally speaking, is about?

A. Yes.

Q. Can you just explain that?

A. It is basically a detailed schedule showing the gross amount that was raised less what was paid to Charles Vista and how the net amount that came into Waste Energy was disbursed. Then what was left over at the

[p.84]

bottom is the $90,000 he was referring to in the e-mail.

Q. I take it these numbers are in thousands?

A. They are in thousands.

Q. As of the end of September 2009, do you know how much cash on hand Waste2Energy had?

A. I can refer to the financial statements.

Q. Let's go back to Exhibit 46, which I believe is in evidence. If you can look at page 4, please?

A. $9,000. $9,007.

Q. I am sorry. So the 9,000 cash line, that is your answer as to how much cash it had on hand as of September 30, 2009, the company?

A. Yes.

Q. All right. You can put that away. Oh, let me ask you one more question. I am sorry, about that same page.

The total assets line says, $905,582 there?

A. Yes.

Q. That was the total assets as of

[p.85]

September 30, 2009?

A. Yes.

Q. And that was an unaudited number. Is that correct?

A. That's correct.

Q. When was this document, this 10-Q filed? If you look at the last page --

A. November 16, 2009.

Q. As of or beginning October 2009, how was Waste2Energy funding its operations?

MR. HANTMAN: I think that was asked and answered, your Honor.

MR. KAUFMAN: I think I asked about September.

JUDGE FOELAK: Objection overruled. Please answer.

THE WITNESS: Could you repeat the question, please?

Q. As of October 2009, how was Waste2Energy funding its operations?

A. During October the company – well, Charles Vista, working with the company, launched date an offering of 12-percent debentures.

[p.86]

Q. If you can look at tab 1, do you recognize this document? It says "Form 10-K Waste2Energy"?

A. Yes.

Q. Can you tell us what this is?

A. This is the annual report filed with the Securities and Exchange Commission which includes the audited financials for the year ending March 31, 2010.

Q. Were you involved in preparing this document?

A. Yes, I was.

Q. What did you do?

A. What did I do with the preparation?

Q. Just very generally.

A. I was involved in developing the financial statements, the footnotes, the write-up of the business.

Q. Would you turn to the last page, please. Is that your signature block there and the date July 12, 2010, what does that mean?

A. That would have been the filing date with the Securities and Exchange Commission.

MR. KAUFMAN: Division offers

[p.87]

Exhibit 1.

JUDGE FOELAK: Hearing no objection, Exhibit 1 is admitted.

(So received in evidence as Division Exhibit 1.)

Q. Please turn to 19. There is a paragraph with heading "We have incurred significant debt to finance our operations to date." You see that?

A. Yes.

Q. The second sentence of that paragraph says "Of this amount, $9,538,113 represents our 12 percent senior convertible debentures which are due one year from the date of issue," et cetera.

My only question is, is that the 12 percent debenture offering you are referring to?

A. Yes, it is.

MR. HANTMAN: Sorry. What page is this on?

MR. KAUFMAN: Page 19 – it is on the top right-hand corner, the page numbers.

We are also putting it up on the

[p.88]

screen.

MR. HANTMAN: Thanks.

MR. KAUFMAN: Sorry, your Honor.

Q. Let me ask you to turn to tab 65, please. This is Division Exhibit 65, which appears to be an e-mail from Craig Brown to Vesselin Mihaylov, V-E-S-S-E-L-I-N, M-I-H-A-Y-L-O-V, dated September 29, 2010, subject W2E diligence item 4, list and contact info of noteholders, and there is an attachment.

Do you recognize this e-mail and attachment, sir?

A. Yes.

Q. Did you send this e-mail on September 29, 2010 with the attachment?

A. Yes.

MR. KAUFMAN: The Division offers Exhibit 65.

JUDGE FOELAK: Exhibit 65 is admitted.

(So received in evidence as Division Exhibit 65.)

Q. Can you explain who Mr. Mihaylov is and why you were sending him this e-mail with the attachment?

[p.89]

A. He was an investment banking associate, I believe, with Charles Vista and was involved there -- I don't recall specifically but there had been some discussions with some third parties that might have had interest in investing or buying the company at the time. And they had requested a list of all the noteholders.

Q. Is the list of noteholders of Waste2Energy the attachment to this e-mail?

A. Yes.

Q. Which notes -- so we are talking about pages 2 and 3 of this document now.

Which notes are listed here? What notes do these noteholders hold?

A. These are principally -- the bulk of the document down to the section that says "Other notes," everything else are the holders of the 12-percent debentures.

Q. So everybody listed above the "Other notes" on this document are holders of those 12-percent debentures that you testified about?

A. That's correct.

Q. And what was the total amount? Can

[p.90]

you tell the total amount that was raised through the sale of these debentures?

A. $10,058,013.

Q. Is that the number that is listed at the bottom of that list?

A. It is.

Q. Did any of these investors who are listed on here as having invested in the debentures, did any of them receive back any of the principal amount of their investment?

A. No.

Q. In 2009, did Waste2Energy have any kind of understanding or agreement with Charles Vista that Charles Vista would raise additional money, if necessary, to repay these debenture holders?

A. Can you repeat the question?

MR. KAUFMAN: Can I ask the court reporter to read back the question, your Honor?

(Record read.)

A. Not that I am aware of.

Q. I am just going to ask you -- so let's look at the second three pages of the document and the headings at the top of each column. I

[p.91]

want to focus on those.

The first one, "Noteholder," what does that mean?

A. That is the individual or entity to whom the note was issued.

Q. By the way, do you know who prepared this chart or the attachment to the e-mail?

A. I maintained and prepared this.

Q. Where did the information come from that you put in the chart?

A. It came from closing documents from each closing transaction that would have been forwarded to me from someone at Charles Vista.

Q. By "closing transaction" you are referring to the individual debenture purchasers?

A. Yes.

Q. And then the second column says "Address." What does that refer to?

A. That was the mailing address provided in the documentation that was sent to us in the closing documents.

Q. So the mailing address for each noteholder?

[p.92]

A. Yes.

Q. And the "Note date," what does that refer to?

A. That was the date of the closing of each note.

Q. And the "Amount," what does that refer to?

A. That was the principal amount of the investment made by the investors.

Q. That was the dollar amount?

A. Dollar amount.

Q. I want to just ask you to describe one example on this list. If you look about three-quarters of the way down or a little further there is a listing for a Roslyn Parmased, R-O-S-L-Y-N, second name P-A-R-M-A-S-E-D. Do you see that?

A. Yes.

Q. So what does this chart show for Ms. Parmased?

A. It shows that she invested $15,000 -- purchased a debenture with a face value of $15,000 on December 18, 2009.

Q. And this is one of the 12 percent

[p.93]

Waste2Energy debentures?

A. Yes.

Q. Let me ask you to turn to tab 54. Exhibit 54 is a series of documents that have the name Roslyn Parmased and also Vishal Goolcharan, G-O-O-L-C-H-A-R-A-N, on them in various places. Do you recognize the documents?

A. Yes.

Q. Can you tell us generally what they are?

A. Yes. This was an example of the documents that were required to be completed by each investor at the time they agreed to purchase these securities.

Q. The 12-percent debentures?

A. The 12-percent debentures.

MR. KAUFMAN: Division offers Exhibit 54.

JUDGE FOELAK: Division 54 is admitted.

(So received in evidence as Division Exhibit 54.)

Q. Can you tell me generally what these documents show?

[p.94]

A. Generally they are – provide the amount of the investment. They have to check what type of accredited investor status they are as an individual firm. It has their contact information, their signature, signature page.

Q. Let's look – and are these all talking about a single investment, these documents?

A. All these are talking about a single investment, yes.

Q. Let's look at the second page. Under A-1 it says "Roslyn Parmased and Vishal Goolcharan." You see that?

A. Yes.

Q. It says "Names of subscribers." You see that?

A. Yes.

Q. Who do you understand them to be in this transaction?

A. They are the subscriber or the purchaser of the security.

Q. And how much did they invest?

A. $15,000.

Q. Is it fair to say that this $15,000

[p.95]

investment that is discussed in these documents, Exhibit 54, is the same one that we looked at on Exhibit 65?

A. Yes.

Q. That is all for that one.

Sir, did you have any direct contact personally yourself, while you were at Waste2Energy, with anyone from Charles Vista?

A. By phone and e-mail.

Q. Who did -- other than e-mail. Let's put e-mail aside for a second. By telephone who did you have direct communication with?

A. Mr. Frank Lorenzo, Mr. Gregg Lorenzo, Vesselin -- the gentleman we just referenced an e-mail from, Vesselin and -- I don't recall anyone else specifically.

Q. Was there a particular person who was your primary contact at Charles Vista?

A. The person I spoke to probably the most during their tenure was probably Mr. Frank Lorenzo.

Q. Did you ever withhold any information about Waste2Energy from anyone at Charles Vista?

A. No, I did not.

[p.96]

Q. Do you know of anyone at Waste2Energy who withheld any information about Waste2Energy from Charles Vista?

A. I do not.

Q. What ultimately happened to Waste2Energy after you left?

A. It was placed into bankruptcy.

MR. KAUFMAN: Your Honor, I am not going to use this witness to do this but I just want to offer Exhibit 53, which are bankruptcy filings for Waste2Energy.

MR. HANTMAN: No problem, your Honor.

JUDGE FOELAK: Exhibit 53 is admitted.

(So received in evidence as Division Exhibit 53.)

MR. KAUFMAN: May I have a moment, your Honor?

JUDGE FOELAK: Yes.

(Pause.)

Q. I don't know if you recall, sir. We can look back -- why don't we look back at Exhibit 7. The paragraph numbered 3. Last phrase says, "This is a never-ending loop that only benefits CV in the short term." Correct?

[p.97]

Do you see that?

A. Yes.

Q. By "CV" I think you said you understood that to mean Charles Vista?

A. Yes, Charles Vista.

Q. Do you have an understanding of why this never-ending loop only benefited Charles Vista in the short term?

A. Well, I think what he was referring to when he wrote that e-mail was the fact that, you know, from every transaction they were generating a commission of approximately 10 percent of each transaction that occurred, and I think that was the reference that he was making there. In some cases -- I mean, I think he felt like they were getting paid from every transaction and...

Q. Thank you.

MR. KAUFMAN: Your Honor, we don't have any further questions on direct. We may have redirect.

JUDGE FOELAK: Would you like a break before we cross-examine?

MR. HANTMAN: I would rather continue

[p.98]

now, get a couple of questions in and then we can take a break.

JUDGE FOELAK: Okay.

CROSS-EXAMINATION

BY MR. HANTMAN:

Q. Now, Mr. Brown, what was your salary at Waste2Energy when you were hired in 2009?

A. 170,000, I believe, annually.

Q. And what were your expenses on the average, your personal expenses, entertainment, travel?

A. Probably 11, $1,200 a month, principally for living expenses. I was traveling from out of town.

Q. Mr. Bohan, what was his salary in 2009?

A. I believe he was at 250.

Q. And this for a company that had terrible financials, that was not making money?

A. I believe that is what his salary was.

MR. KAUFMAN: Objection.

Q. Excuse me?

A. I believe that is what his salary was.

Q. At the very beginning when you started

[p.99]

with the company they were in poor financial condition. Correct? That is your testimony; right?

A. They were. Yes.

Q. So you were making – how much did you say you were making?

MR. KAUFMAN: Objection. Asked and answered.

JUDGE FOELAK: Your objection is sustained.

Q. Now, you looked at – actually, let's jump around a little bit. With respect to Roz Parmased I think it is, Exhibit 54, did you ever meet her?

A. I did not.

Q. Ever speak to her?

A. I did not.

Q. You ever look at any e-mails from her?

A. I did not.

Q. Did you ever send her any e-mails?

A. I did not.

Q. Do you know who she might have talked to between October 2009 and December 2009?

MR. KAUFMAN: Objection.

[p.100]

JUDGE FOELAK: What is the basis for your objection?

MR. KAUFMAN: Lacks foundation.

MR. HANTMAN: It is fair enough. He either knows or doesn't know.

JUDGE FOELAK: Go ahead and answer. Either you know or you don't know.

THE WITNESS: Can you repeat the question, please?

Q. There was an e-mail she purportedly received sometime in October 2009. Correct?

MR. KAUFMAN: Objection.

Q. If you know. Do you know whether she ever received an e-mail from Mr. Francis Lorenzo at the request of Gregg Lorenzo and a guy named Spiro in October 2009, yes or no?

A. I do not know.

Q. You don't know that. So you don't know why she and her husband or her boyfriend, this person Vishal, you don't know why they invested $15,000, do you?

MR. KAUFMAN: Objection.

JUDGE FOELAK: You know, Mr. Hantman, reliance is not an element of a securities fraud

[p.101]

case that is an enforcement case. I thought I would mention that.

Q. I am asking, do you know why they sent the money in?

A. I do not know.

Q. Do you know if they spoke to anybody between October and December? Do you know why they waited until December to invest money?

MR. KAUFMAN: Objection. This witness can't testify what was in the mind of another person.

JUDGE FOELAK: Sustained.

Q. Now, there was a list different noteholders. I believe it is Exhibit 65. Do you want to take a look at that, please? About the 10th line down it has a Mr. Benkovsky, does it not, and shows October 1, 2009?

A. It does.

Q. You were questioned about this on direct examination. Correct, about this list?

A. I was.

Q. And was this $2 million, as far as you know, an investment or a debenture?

A. It was a debenture.

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Q. And this was in October 2009. Did you ever meet Mr. Benkovsky?

A. Did not.

Q. Do you know who he is?

A. I do not.

Q. Had you ever heard his name?

A. I have heard his name.

Q. And who mentioned his name to you?

A. I heard his name during the course of my tenure there because he was a significant investor in these securities.

Q. And in September of 2009, look at Exhibit Number 7 if you will, please. On paragraph number 1 it says that the bridge would have covered OPEX. That is operating expenses. Correct?

A. Yes.

Q. "For four months if we did not have to incur repayment of notes and significant repayments to accounting, audit and legal firms." You see that. Correct?

"It was always indicated that these would be paid out of continuing equity raise and as you can see if this were the case we would

[p.103]

have enough money for an additional two months at least."

Is that correct?

A. Yes.

Q. So is it fair to say that when this bridge money came in, these debentures, as far as the investors knew, it would have gone to do something to help enhance the business of Waste2Energy? Yes or no?

MR. KAUFMAN: Objection. The question was, I think, "as far as investors knew." This witness cannot testify about what other people knew.

MR. HANTMAN: Well, he testified as to what Mr. Lorenzo knew.

MR. KAUFMAN: No, he hasn't, your Honor, but in any event.

JUDGE FOELAK: Your objection is sustained.

Q. Let me ask you, do you know who was paid -- what accounting firm was paid out of the -- out of the raise?

A. There were two firms paid. Marcum, which was the firm that actually did the audit,

[p.104]

as well as Citrin Cooperman, which was the firm that provided accounting support for the SEC filings, particularly while there was no accounting personnel on staff prior to my arrival.

Q. Where are they located?

A. In Manhattan.

Q. Who are the principals of those two firms?

A. David Bukzin was the principal at Marcum. And Corey Massella was the main contact I had at Citrin Cooperman.

Q. Do you know where in Manhattan they are located?

A. Not specifically.

Q. Who were the audit and legal firms? You testified to this. It was read into the record. What audit and legal firms was this referring to?

A. Audit firm was Marcum, who I just referenced.

Q. The legal firm?

A. Sichenzia Ross Friedman & Ference.

Q. When Mr. Benkovsky made an investment

[p.105]

in August 2009, do you know whether he was informed that this money would be used to pay accountants and lawyers?

A. I don't know.

Q. Now, with respect to Exhibit 55 is there anything in that document which is inaccurate?

MR. KAUFMAN: Your Honor, that is a very broad question.

JUDGE FOELAK: It is indeed.

MR. KAUFMAN: It is overbroad and not fair to the witness.

MR. HANTMAN: He testified --

JUDGE FOELAK: My concern is, it is a contract. It is not like a statement of facts or something, as far as asking him whether there is something inaccurate.

Q. When is the earliest time that you realized, as one of the leading people at Waste2Energy, that this contract had little or no value?

A. Probably when -- as I got my -- was getting up to speed with the business in July, August 2009, after I joined.

[p.106]

Q. And what is the earliest -- do you have a document which you sent directly to Mr. Lorenzo which said that this contract had no value?

MR. KAUFMAN: Can I have the question read back? I am sorry.

Q. Do you have any document -- it doesn't have to be any document that is part of an exhibit list, okay? This is cross-examination.

Do you have any document that you prepared which you sent to Mr. Frank Lorenzo in which you said that this contract is of little or no value, yes or no?

MR. KAUFMAN: Objection.

A. I don't recall.

Q. Excuse me?

A. I don't recall.

Q. Do you know if anyone from Waste2Energy ever sent Mr. Lorenzo a document that said this contract, referring to Exhibit 55, is of little or no value? Yes or no?

A. I can't speak on behalf of other individuals.

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Q. With respect to Exhibit 46, the Form 10-Q for November 2009, as far as you know, is that accurate or is it false? Is it true or false?

A. What is the exhibit?

Q. You signed it.

A. Yes, it is accurate.

Q. What led you to believe that the intangible of $10 million was worth something then?

MR. KAUFMAN: I am sorry. Which document are we talking about?

JUDGE FOELAK: 46.

A. There was no intangible in that document.

Q. So it doesn't refer to $10 million?

A. This September 30, 2009 10-Q? There was no intangibles on the balance sheet.

Q. When were intangibles first put on the balance sheet?

A. When were they first put on?

Q. Yes.

A. During 2008 upon the acquisition of a couple businesses that the company had acquired.

[p.108]

Q. So you are saying as early as 2009 it was no longer listed as an asset?

MR. KAUFMAN: Objection. Asked and answered.

JUDGE FOELAK: Your objection is sustained.

Q. The write-down was when? In July of 2009, of this $10 million?

A. It was written down and included in the audited statements for the year ending March 31, 2009.

Q. Now, Mr. Benkovsky, he invested money, he bought a debenture in August 2009. Correct, according

—

MR. KAUFMAN: Objection.

JUDGE FOELAK: I think that list said --

MR. KAUFMAN: October 1st.

JUDGE FOELAK: Yes.

MR. KAUFMAN: I think that is what the document said.

JUDGE FOELAK: That is what the document said.

Q. Well, Benkovsky -- I am a little

[p.109]

confused. You are saying --

MR. KAUFMAN: Your Honor, the only evidence that is in so far of when Mr. Benkovsky purchased is Exhibit 65, which I think the witness was shown, and the line for Mr. Benkovsky, if this is what is being referred to, says October 1, 2009.

MR. LORENZO: That is when the notes were issued. He invested --

MR. KAUFMAN: Your Honor, we would object to Mr. Lorenzo speaking out of turn.

JUDGE FOELAK: He can testify when he testifies.

Q. Do you know when Mr. Benkovsky invested, yes or no?

A. No.

Q. I won't give you a date. Do you know when he invested?

A. Based on the schedule, October 1, 2009.

Q. And did you ever tell him before then that there was going to be a write-down of $10 million in the asset?

A. Did I tell who?

[p.110]

Q. Mr. Benkovsky.

A. I think I already mentioned I never spoke to him.

Q. You never met Mr. Lorenzo in person. Correct?

A. Correct.

Q. How many times did you speak to him?

A. I am not certain.

Q. Excuse me?

A. I am not certain.

Q. More than once?

A. Yes.

Q. More than ten times?

A. Yes.

Q. More than 20 times?

A. Probably, yes.

Q. Do you have any memorandum reflecting your conversations with him?

A. I don't recall.

Q. Well, before you came here today, when did you first speak to the SEC about being a witness today?

A. Six months ago.

Q. Did you contact them and volunteer or

[p.111]

did they contact you?

A. I was contacted.

Q. Who contacted you?

A. Mr. Kaufman.

Q. And what did he say to you?

A. He just asked me if I can come in and talk to hem about this case.

Q. Were you concerned that you were being investigated?

A. No.

Q. Have there ever been any charges filed against you?

A. No, there have not.

Q. Any charges filed against Mr. Bohan?

A. Not that I am aware of.

Q. Any lawsuits filed against W2Energy that you know of, any civil lawsuits?

A. Not that I am aware of.

Q. Are you named a party in any lawsuits?

A. No.

Q. Mr. Bohan?

A. Not that I am aware of.

Q. Do you know if the company has professional liability insurance?

[p.112]

A. Yes, they do.

Q. With whom?

A. They had a D and O policy. I don't recall the carrier. It may have been Travelers. I am not certain.

Q. Do you know who the insurance broker was?

A. A company called William Gallagher Associates.

Q. Where are they based?

A. Atlanta, Georgia.

Q. Now, with respect to what you testified to in Exhibit Number 7, in paragraph number 1, was all the money that was raised in this bridge -- well, do you know what amount this is referring to with respect to "the bridge would have covered"? When it says "the bridge" do you know what number that is referring to?

A. I think it is the 1.5 million on the subsequent page.

Q. Was all that 1.5 used to pay accountants and lawyers and auditing fees?

A. If you can scroll to the next page I think it -- there is a schedule.

[p.113]

MR. KAUFMAN: Just to be clear, your Honor, I think what is referred to is 2.5 million, just for the record.

JUDGE FOELAK: It does says 2.5 million.

Q. 2.5 million, and then you say on the last page is how it was paid out? Look at the use of proceeds. It says "1.5 million bridge loan"?

A. Right. That is what I am looking at.

Q. This is how the 1.5 was paid out?

A. Yes.

Q. And this includes the amount that was paid to the lawyers and the legal? That is 295,000?

A. Yes.

Q. Was W2Energy, they were aware that if they gave information to Charles Vista which was negative, that would impact on the ability of Charles Vista to raise money from investors. Correct?

MR. KAUFMAN: Objection. I think the question was about what Waste2Energy knew. Again -- and it is also a compound question.

[p.114]

Again, this witness can't testify about what Waste2Energy knew about anything. He can testify about what he knew or didn't know.

MR. HANTMAN: Fair enough.

Q. Did you ever discuss with Mr. Bohan that it is better not to reveal certain information to Charles Vista prematurely because it would cut off the gravy train?

A. No, I did not.

Q. With respect to this $10 million write-off, did you have any internal memorandum, you personally, any internal memo which referred to this $10 million write-off, yes or no?

A. Was there a memorandum?

Q. Yes.

A. Yes.

Q. Do you have it here today?

A. I don't have it with me. I don't know if the Securities and Exchange Commission has it. I am not sure.

Q. Aside from a memo on that -- what was the date of that memo, if you recall, that you have personal knowledge of?

A. There was a memorandum written that

[p.115]

was done at the request of our audit firm during the course of the audit sometime in September of 2009 basically just going back to historically the creation of those intangibles through several acquisitions the company did and what transpired to result in the impairment of those assets.

Q. So that was in September. Is that the earliest that you recall a memorandum was prepared with respect to this $10 million write-off?

A. Yes, because I was personally involved in writing that memorandum.

Q. Okay. And that is September what?

A. 2009.

Q. Do you know who prepared this memo?

A. I did the bulk of the work.

Q. Did you send that memo, that internal memo to Gregg Lorenzo?

A. I don't recall.

Q. Did you send it to Francis Lorenzo?

A. I don't recall.

Q. Did you pick up the telephone at or about the time this memo was prepared and say,

[p.116]

"Hey, Frank, listen, this is pretty important. I am preparing an internal memorandum that says we are

going to write off $10 million"? Did you have that conversation with Mr. Lorenzo?

A. There was conversation, at least one because they were very interested in how quickly we could get the audit completed so they can begin the marketing of these securities. As such, we updated them that we had a pretty significant issue going on that we were evaluating to complete the audit and it had to do with the impairment of these assets.

Q. And when was the date of that conversation?

A. It was probably in mid-September I am guessing. I don't have an exact date.

Q. Do you have a proof of this conversation?

MR. KAUFMAN: Objection.

Q. Other than you testifying you had this conversation?

MR. KAUFMAN: Objection to "proof." It is a legal term.

Q. Well, this would be a pretty important

[p.117]

conversation, would you not agree?

A. I agree.

Q. Important enough to reduce to writing?

A. It had a memo in writing.

Q. And is that memo a part of the exhibits that you have looked over this morning?

A. I haven't had it looked over this morning, no.

Q. And you don't have that memo with you?

A. I don't have any records with me, no.

Q. This telephone conversation --

MR. KAUFMAN: Your Honor, if it would help, Exhibit 13, I think, is the memo. That would be up to the witness to testify to.

MR. HANTMAN: Thank you.

Q. I am looking at Exhibit 13 and this appears to be -- it says "Memo to file." Is that correct?

A. Yes.

Q. It doesn't indicate that this was sent to anybody, does it?

MR. KAUFMAN: Asked and answered, your Honor.

MR. HANTMAN: Well, it can be because

[p.118]

he just looked at it for the first time with Mr. Kaufman assisting me --

JUDGE FOELAK: Correct. You can go ahead and answer.

A. This memo was sent to our auditors and to Citrin Cooperman as well as to internal management. I don't recall if it was sent to Charles Vista.

Q. And was the reason it wasn't sent to Charles Vista you didn't want them to cut off the gravy train?

MR. KAUFMAN: Objection.

JUDGE FOELAK: You can answer it. Your objection is overruled.

A. No, that is not the reason.

Q. Well, then, why didn't you send it to them?

A. This was an internal document --

MR. KAUFMAN: Objection. He didn't say he didn't send it. He said he didn't remember.

A. This document was prepared at the request of our audit firm, and that was principally who -- we were trying to get

[p.119]

resolution on this impairment issue. Again, I don't recall if it was sent to Charles Vista, but they were aware of the issue.

Q. When you say they were aware of the issue, do you have any documentation from Mr. Lorenzo that says "I am aware of this issue of a $10 million issue," yes or no?

A. I don't --

Q. Yes or no?

A. I don't recall.

Q. Before you came here today, didn't you look at your records since one of the elements of what Mr. Lorenzo is accused of doing is misrepresenting this $10 million write-down?

MR. KAUFMAN: Objection, your Honor. That is not a question.

MR. HANTMAN: This is a question.

MR. KAUFMAN: It is a very argumentative question.

JUDGE FOELAK: It is. Your objection is sustained.

Q. Before you came here today, were you aware whether Mr. Lorenzo was aware or not of a $10 million write-down as a material issue, yes

[p.120]

or no?

MR. KAUFMAN: Objection.

JUDGE FOELAK: Your objection is overruled. If you understand the question.

A. Can you repeat the question, please?

Q. When you spoke to Mr. Kaufman, did he indicate to you what the nature of the charges against Francis Lorenzo were? Did he go over the charges?

A. Not specifically. Not in detail, no.

Q. You just spoke about it generally?

A. Yes.

Q. Did you ever tell him that in your opinion Mr. Lorenzo definitely knew about a write-down of $10 million in the intangible asset? Did you tell him that?

A. I told him that we had communicated to Charles Vista that this write-down was being evaluated and was the key to finalizing the audit of the 3/31/2009 financials.

Q. I am not quite sure you answered the question.

MR. HANTMAN: Can you read the question, please.

[p.121]

(Record read.)

Q. That is either yes or no.

A. Did I tell who that?

Q. Mr. Kaufman.

A. Yes. I told him that Charles Vista was made aware of that.

Q. Did you tell him that Mr. Francis Lorenzo was aware of it?

MR. KAUFMAN: Objection.

Q. Yes or no?

A. I don't know whether I specifically mentioned Mr. Frank Lorenzo or Charles Vista or Mr. Gregg Lorenzo.

Q. As you sit here today, under oath, do you have any documentation from you, from you personally to Mr. Lorenzo, that says, "Frank, this $10 million intangible has been written off"? Yes or no?

MR. KAUFMAN: Your Honor, there is Exhibit 19.

MR. HANTMAN: I have the right to ask this witness himself. I think it is improper to suggest what he should be looking at when I am just asking him a question.

[p.122]

JUDGE FOELAK: Okay. You can answer the question if you remember it.

A. I don't recall. I did not bring any records from that company with me today. I did not bring records with me.

Q. Well, other than this one Exhibit 19, which I am not quite sure what this is. It doesn't look like an e-mail.

Let's look at 19 for a second, since this is the government's case.

MR. KAUFMAN: Your Honor, I would object generally to editorial comments by counsel about our case when the witness is on the stand. It is proper for opening or closing.

JUDGE FOELAK: Correct. He is not sequestered at the moment.

Q. Who prepared this document? You?

A. Yes.

Q. When did you prepare it?

A. October 5, 2009.

Q. October 5th. You prepared this for whom?

A. For Andre Zdanow.

Q. Other than this document, is there any

[p.123]

other document which refers to this intangible write-off that you are aware of?

A. Are there other documents? Yes.

Q. Other than this? You have those documents with you?

A. There were documents that were filed with the Commission that refer to this. October 1st, that we reviewed earlier.

Q. And sometime -- October when?

A. The amended 8-K and 10-Q that described this in great detail were filed October 1st.

Q. Did you have any conversations with Mr. Lorenzo personally about this memo?

A. About this memo?

Q. Yes.

A. I don't recall.

MR. KAUFMAN: I am sorry. Which memo are we talking about? I am confused.

JUDGE FOELAK: Are you referring to Exhibit 19, Mr. Hantman?

MR. HANTMAN: Exhibit 19.

MR. KAUFMAN: That is an e-mail. Okay.

[p.124]

Q. Now, with respect to purchase orders and letters of intent, did you ever discuss with Mr. Lorenzo what orders, if any, W2Energy had, yes or no, you personally?

A. Yes.

Q. When?

A. I don't recall specifically when, when I would have had those conversations. But I know there was conversations -- a lot of conversations and a lot of interest about the letter of intent that ultimately was signed with St. Martin by Waste2Energy.

Q. What was the nature of the conversation?

A. I don't recall spccifically but wanting to know the value of the contract -- potential contract. It wasn't a contract. It was a letter of intent. The value of it, when they thought it would get to a point where it might go to contract. Things to that nature.

Q. What was the earliest that you had a conversation that it was not going to come to contract?

A. I don't know that I ever had a

[p.125]

conversation with Mr. Lorenzo. I don't think that occurred until after he had left Charles Vista.

Q. So the subject matter of purchase orders or letters of intent for over 43 million, you are saying,

happened after Francis Lorenzo left Charles Vista? Is that your testimony?

MR. KAUFMAN: Objection. I don't think that is what the witness said.

Q. I am asking, is that your testimony? Yes or no?

A. I was just referencing any comments about that letter of intent with St. Martin.

Q. That would have been what period of time?

A. That happened sometime in 2010. Mid to late 2010 I believe.

Q. I don't want to put words in your mouth. Maybe it is unclear to me.

Is it your testimony that any conversations over purchase orders and letters of intent would not have been discussed until 2010 sometime?

A. That is not what I testified. You

[p.126]

asked specifically when did I tell him that the letter of intent was not going to convert to a contract.

Q. Right.

A. And I told you that I don't believe I ever had that conversation because that occurred after he was no longer employed by Charles Vista.

Q. Okay. That is fine.

With respect to whether Charles Vista agreed to raise additional monies or not to repay the debenture

holders, did anyone from Charles Vista ever tell you they were not going to raise money?

A. No.

Q. You don't know whether they intended to raise money or not, do you, sir?

A. No.

MR. KAUFMAN: Objection.

Q. You don't know whether they intended to raise money or not, do you, sir?

JUDGE FOELAK: Wait. There is an objection.

MR. KAUFMAN: Again, he is asking this

[p.127]

witness to testify about someone else's intent. It is really not a proper question.

Q. Weren't you asked on direct examination whether you were aware of an agreement between Waste2Energy and Charles Vista that they would raise additional monies to pay debentures? Do you recall being asked that question?

A. Yes, I recall that.

Q. Okay. But that doesn't mean that Charles Vista might not have agreed to repay debentures to certain individuals?

MR. KAUFMAN: Objection.

Q. Yes or no?

JUDGE FOELAK: It is kind of opaque and confusing.

Q. Let me ask you, do you know whether Gregg Lorenzo – he is the principal of Charles Vista; right?

A. Right.

Q. He is the main guy?

MR. KAUFMAN: Objection.

Q. In your mind, was he the main principal?

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A. That was my understanding.

Q. Was it your understanding that he was higher up than Francis Lorenzo?

A. That was my understanding.

Q. Was it your understanding that he was making the bulk of any monies generated from being the investment banker for Waste2Energy?

A. I didn't have knowledge of that.

Q. So as you sit here today, do you know what Gregg Lorenzo ever told debenture holders of Waste2Energy?

MR. KAUFMAN: Objection.

MR. HANTMAN: He can answer whether he knows. He either knows or doesn't know.

MR. KAUFMAN: If defense counsel is asking about a conversation between two people that this witness was not a part of, how can he testify about it?

Q. Did Gregg Lorenzo ever tell you that he did not promise people that he would raise monies to pay debentures? Did Gregg Lorenzo tell you "I am not going to raise money to pay these debentures holders"?

A. No.

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Q. Did Gregg Lor -- did Francis Lorenzo ever say that nobody had agreed to pay these debenture holders money?

MR. KAUFMAN: Objection. I just don't understand the question.

MR. HANTMAN: I have a lot more questions, your Honor, but if you want to take a lunch break, we can do that?

JUDGE FOELAK: That is a good idea. Is one hour sufficient?

MR. HANTMAN: That is fine.

MR. KAUFMAN: Thank you, your Honor, yes.

JUDGE FOELAK: So until a quarter of 2 then.

MR. HANTMAN: Your Honor, if I can, before going off the record, if we contact one or two of our character witnesses and they can make it after lunch, could we take their testimony out of order to accommodate?

JUDGE FOELAK: I don't know. This gentleman has travelled here. They could come tomorrow morning or whatever you want.

MR. JANGHORBANI: Your Honor, we

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object to that. We have a very small case in chief. We have Mr. Brown, Mr. Rothe for less than ten minutes and Mr. Lorenzo. We are entitled to put on our case without taking witnesses out of order because they didn't prepare.

JUDGE FOELAK: Besides, they are less likely to come this afternoon than later tomorrow.

MR. HANTMAN: To accommodate your Honor's schedule, if we don't finish today we will continue tomorrow morning at 10 o'clock?

JUDGE FOELAK: Correct. We have all week.

MR. HANTMAN: Thank you very much.

(Luncheon Recess.)

AFTERNOON SESSION

JUDGE FOELAK: I want to remind you you are still under oath from this morning.

CONTINUED CROSS-EXAMINATION

BY MR. HANTMAN:

Q. Mr. Brown, as the chief financial officer of a public company getting money from the public, what were your responsibilities and

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duties?

A. To basically oversee the use of those assets and safeguard them once they are in -- my responsibilities within this particular company were somewhat constrained only because the principal of the company, who was the sole director of the company, and Mr. Bohan, who we spoke of earlier who is CEO, really handled the bulk of the relationship, I would say, with Charles Vista in terms of dialogue surrounding the financings.

Q. Well, do you know of any reason why Mr. Bohan is not here today?

MR. KAUFMAN: Objection.

Q. Is Mr. Bohan alive? Is he alive?

JUDGE FOELAK: That is a fair question. Is he alive?

A. Is he alive? Yes, as far as I know he is alive.

Q. Do you know where he is?

A. I don't know where he is today, no.

Q. Do you know whether there is any physical impediment for him to be here?

A. I don't know.

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Q. Do you know whether he spoke to the SEC?

A. I don't know.

MR. KAUFMAN: Objection.

Q. Did you ever ask him whether he spoke to the SEC?

A. No.

MR. KAUFMAN: Objection. Calls for hearsay.

MR. HANTMAN: That is not hearsay, whether he spoke to somebody.

JUDGE FOELAK: No. He asked him -- you can answer that question, whether you asked Mr. Bohan whether he spoke to the SEC.

A. No, I have not asked him if he spoke to the SEC.

Q. Does he know that you are here today?

MR. KAUFMAN: Objection.

Q. Did you have any conversations with him about you being here today?

MR. KAUFMAN: Objection.

JUDGE FOELAK: Go ahead and answer.

A. He called me several days ago. He had been trying to call me for several weeks, and he

[p.133]

asked me if I was still involved with this case.

Q. What did you tell him?

A. I said I was and I didn't go any further.

Q. Did you tell him what your involvement was?

A. I didn't go any further.

Q. What is your educational background?

A. I have a finance degree from Clemson University.

Q. Okay.

A. I am a CPA.

Q. Okay. And after college, can you briefly give us your work experience?

A. Yes. I worked in public accounting with PriceWaterhouse three and a half years, three or three and a half years. Then I went and worked in a variety of public and private companies over the course of the next 15 years, publicly traded holding company, an insurance broadcasting operations, a pulp and paper manufacturing company for two years, a life sciences company for about seven years, pharmaceutical company.

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After we sold the life sciences company, a pharmaceutical company for about a year. And then Waste2Energy.

Q. Are you aware of whether there was a contract between Charles Vista and W2E?

A. Was there a contract between Charles Vista?

Q. A contract for Charles Vista to raise money --

A. There was an agreement, I recall, that specified the term of their compensation, yes.

Q. And do you know whether that agreement provided that W2E would disclose any material changes in the financial situation of the company?

A. I don't recall but that would be standard within that type of agreement.

Q. Would a write-down of $11 million be a material change in the financial viability of W2E, yes or no?

A. Yes.

Q. Do you know what an indenture -- I am sorry. Do you know what a debenture is?

A. Yes.

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Q. What is a debenture?

A. It is a securities and obligation to repay a debt.

Q. In this particular case the debentures were a priority so that in the event of the liquidation of the company the people who hold the debenture would get paid first, if you know?

A. I believe so, yes.

Q. So --

A. They were senior.

Q. They were senior. Okay. When you say "senior," what does that mean? Can you define what a senior --

A. Preference over non-senior securities. They would take preference over non-senior securities.

Q. So when Mr. Benkovsky or other people on the list, when they were making their investment, do you know whether they were advised of this imminent material change in the financial condition of W2E, yes or no?

MR. KAUFMAN: Objection. It is a vague question. Advised by whom?

Q. Advised by you?

[p.136]

A. No.

Q. Do you know if they were advised by anyone?

A. I don't know.

Q. Now, you had stated that you began work on what? The audit of W2E in July of 2009?

A. Yes.

Q. And who worked with you on this audit?

A. Well, it was myself principally representing the company's personnel, and the staff at Citrin Cooperman. And, obviously, we were working with the staff at Marcum as well.

Q. Who were some of the staff you were working with in July 2009 at those two accounting firms?

A. I don't remember all the specific names. Citrin Cooperman, the primary gentleman was Corey Massella, and he had some staff personnel whom I don't remember their names today.

Marcum, the senior manager was a guy named John Klenner we worked with quite a bit. And I don't remember the staff persons under him at this point.

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Q. Did W2E have a board of directors at or about July 2009?

A. Yes.

Q. Who was on the board of directors?

A. Just Chris Taylor.

Q. Who is that?

A. He was the founder of the company.

Q. How old is he?

A. How old is he?

Q. Yes.

A. Now or then?

Q. Now.

A. I would guess -- I would guess -- I don't know his birthday -- he is maybe around 70.

Q. Where does he live?

A Last I know he lived in New York when I was with the company.

Q. When you say last you know, he travels like from state to state?

A. I haven't kept up with him since I left the company.

Q. When was the last time you spoke to him?

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A. 2010.

Q. When is the first time you told him that there was going to be a write-off of $11 million of the company?

A. 2009.

Q. When in 2009?

A. He was part of the discussions going back to August and September of 2009.

Q. Do you have any documentation with you now memorializing the discussions with the person on the board of directors in July, August 2009?

A. Unless they are in this binder, I don't have anything with me, no.

Q. Did the SEC ask you if you had any documentation with respect to this write-off of $11 million?

A. No.

Q. Did they ask you to supply it?

A. No.

Q. Do you have any working papers with respect to any discussions in July of 2009 concerning this $11

million write-off which would have a devastating impact on the holders

[p.139]

of these debentures?

A. No.

Q. You don't have them here, or you don't have any at all?

A. I did not take company records with me when I left the company so I don't have any at all.

Q. Who has those company records if you know?

A. I don't know.

Q. Do you know whether they were lost or stolen?

A. I don't know. I don't know.

Q. Who at the company would have these records of discussions concerning this $11 million write-off in July or August of 2009? Who would have that if you know?

A. There is no one left at the company so I couldn't tell you that.

Q. Well, when did the government contact you with respect to this case?

A. Probably middle of 2011.

Q. Was there a company then?

A. I don't recall when it was put into

[p.140]

bankruptcy but there may have still been at the time.

Q. So in July or August there were discussions concerning write-off of $11 million. Correct?

A. Yes.

Q. Is there any reason nobody at Charles Vista was notified in July or August of this imminent disastrous situation?

MR. KAUFMAN: Objection, your Honor. It assumes testimony not in evidence. I think it might even contradict testimony in evidence.

JUDGE FOELAK: Mr. Hantman?

MR. HANTMAN: I can rephrase it.

JUDGE FOELAK: Okay.

Q. Let's forget the word disastrous, okay? Were there any discussions with anyone in Charles Vista in July of 2009 concerning the potential write-off of $11 million?

MR. KAUFMAN: Discussions between who?

Q. Between you and Charles Vista?

A. In July of 2009?

Q. Yes.

A. I don't recall.

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Q. Well, that would be pretty important, would you not think so?

MR. KAUFMAN: Objection. Vague, argumentive.

JUDGE FOELAK: Your objection is sustained.

Q. Do you know whether anybody had any discussions with Charles -- Charles Vista w as your investment banker, correct?

A. They were.

Q. And they are trying to raise money for you. Correct?

A. Correct.

Q. And they are talking to outside people from the public who are going to be making investments in the company. Correct?

A. Right.

Q. Okay. So, the write-off of $11 million would be an important thing for your investment banker to know of. Yes or no?

A. Yes.

Q. So in July of 2009 -- correct me if you have answered this before -- did you tell anyone at Charles Vista you think you are

[p.142]

writing off $11 million? Yes or no?

A. I don't recall in July of 2009 if I did or did not.

Q. And you have none of the work papers here from July 2009?

MR. KAUFMAN: Objection. Asked and answered. I think this is --

JUDGE FOELAK: Objection sustained.

Q. What about August 2009? Did you have any conversations with anyone from Charles Vista?

A. I don't --

MR. KAUFMAN: About anything at all?

MR. HANTMAN: No. About this write-off of $11 million.

A. I don't recall specifically if I did in August but I know as we got -- as I got more into the process and the issues and the discussions with our audit firm, that's when I started to have more conversations with everybody involved.

Q. Well, in fact, isn't it true, sir, that the auditing firm would not sign off on your financial statements and leave the

[p.143]

$11 million on there?

A. I don't recall being told that by the audit firm, no.

Q. Isn't it a fact that the auditing firm told you that with respect to this $11 million, $11 million valuation on goodwill, that they could not in good faith sign off on

it because it should be written down to zero? Didn't they tell you that, sir?

A. I don't recall if they did or did not.

Q. You are not saying they didn't tell you. You are just saying you don't recall if they told you?

A. I don't recall. I don't recall them saying that.

Q. In fact, isn't it true, sir, that you and the head of the company discussed that you would delay notifying Charles Vista of this write-off as long as possible so that you could get more money from them --

MR. KAUFMAN: Objection.

Q. -- in order to pay off bills?

MR. KAUFMAN: Objection. Asked and answered and --

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JUDGE FOELAK: I am not sure it was. Go ahead and answer if you remember.

A. No.

Q. Well, in September -- we talked about July, we talked about August. Now in September when, if any, was your first conversation with anyone at Charles Vista concerning this write-off?

A. I don't recall a specific date but it was probably in mid-September, in that time frame. Around the time that memo was being put together and finalized, reviewed through with our auditors, getting consensus

on the fact that we were going to impair that entire asset.

Q. Don't you think there was an obligation to notify your investment banker that you are even thinking about writing off the largest single asset of W2E?

MR. KAUFMAN: Objection. I think it's been asked and answered.

MR. HANTMAN: I don't think he has answered this question. It is critical.

JUDGE FOELAK: It is argumentative. You are asking him whether it was

[p.145]

material, which I think he's already answered.

Q. Once you decide you are going to write off -- well, did you discuss with Charles Vista whether you should write off this asset of $11 million?

A. No.

Q. So that would be a decision you would make on your own?

A. That would be a management decision and in discussion and reaching agreement with our audit firm. Yes.

Q. And once you made that decision, you would naturally amend the PPM. Correct?

MR. KAUFMAN: Objection. I don't think -- I don't think a PPM has been discussed before. It is not clear what the question is.

JUDGE FOELAK: Perhaps you should lay a foundation.

MR. HANTMAN: That is a good point.

Q. Are you aware of any private placement memorandum that was prepared by W2E for the purpose of raising monies, yes or no?

A. Yes.

Q. And do you know whether – and as a

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chief financial officer and somebody with a lot of experience and somebody who has worked with public companies, would the fact that an $11 million asset was going to be written off to nothing, would that be something which should be reflected in any PPM? Yes or no?

A. Yes.

Q. Do you know whether the PPM was ever amended to reflect that write-off and if so when?

A. I believe it was. Certainly the incorporation of the final set of financial statements into the PPM, which was an integral part of that document, that change was made.

Q. When?

A. When the financials were finalized on or about end of September, 1st of October.

Q. The end of September.

A. The amended SEC filing was October 1st.

Q. Was when?

A. October 1st.

Q. Now, who was on the board of directors besides that one individual you mentioned?

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A. I believe that was it.

Q. There was only one member of the board of directors?

A. I believe that was it. Just the one.

Q. Are you aware whether any board of director meetings were held in July, August or September of 2009?

A. I don't recall.

Q. Do you know whether it -- do you know whether any board of director meetings were held?

A. I don't recall.

Q. Did you attend any board of director meetings?

A. I did not.

Q. Do you know whether minutes were kept of board of director meetings?

A. I don't know.

Q. So then if there was a board of director meeting, the only person who would show up would be one person?

MR. KAUFMAN: Objection.

A. I don't know.

Q. Have you ever seen any minutes of

[p.148]

board of director meetings?

A. I don't recall.

Q. Aside from the internal memorandum -- well, let me ask you this. I direct your attention to Exhibit 30 if you don't mind, sir. Do you see it?

A. Yes.

Q. This was prepared -- well, on August 19, 2009 you wrote "For your information, as you know we filed a 12B-25 last week," and you are continuing to work on 3/31 numbers and you go on and on.

When you filed the 12B-25 last week, did that include the fact that you were writing off $11 million in assets? When I say "you," the company writing off $11 million in assets? Yes or no?

A. Did that filing include?

Q. Yes.

A. The fact?

Q. Yes.

A. I don't recall. I think that filing was just a notification that we were late in putting the exchange on notice or FINRA on

[p.149]

notice that we were late in our filing.

Q. Don't you think people should be put on notice that you are going to write off $11 million when people subsequently are putting in millions of dollars?

MR. KAUFMAN: Objection. It is argumentative.

JUDGE FOELAK: 12B-25 is just a late notice. You don't have to answer. The question is not related to the 12B-25.

Q. Is there any reason why in this August 19th memo or e-mail that you don't mention about the write down of the $11 million?

A. Is there any reason I didn't mention it?

Q. Yes, the potential write-down of $11 million, any reason why it is not mentioned in this e-mail of August 19, 2009?

A. I don't know of any reason it wasn't mentioned. It wasn't intentional or unintentional I am sure. I was answering Tom Rose's question.

Q. And Tom Rose was who?

A. He was an attorney at Sichenzia Ross.

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Q. Who did he represent?

A. He was securities attorney for Waste Energy.

Q. Exactly. And he said to you, in terms of the second page of that exhibit, where it says, "What can we do to get the Q filed," that was written by Mr. Rose or Ross?

A. Yes.

Q. And then he goes, "I don't see how CV --" that is Charles Vista?

A. Yes.

Q. "-- can sell anything when the company isn't current in its filings." You see that?

A. Yes.

Q. Then he says, "Are they aware this is coming?" You see that?

A. I see it.

Q. Did you read it at the time he sent that to you?

A. Yes.

Q. And did you respond to him?

A. I did respond.

Q. And what did you respond?

A. Scroll up, please?

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MR. KAUFMAN: Your Honor, the e-mail speaks for itself if that is what the question is.

JUDGE FOELAK: It does.

Q. Well, why didn't you mention about potential write-down of the $11 million?

MR. KAUFMAN: Objection. Asked and answered.

JUDGE FOELAK: Has it been asked and answered?

MR. KAUFMAN: Yes.

MR. HANTMAN: Not with respect to this chronological order I am going in.

MR. KAUFMAN: The question is why in this e-mail exchange did you not talk about that, and the witness answered the question.

JUDGE FOELAK: Yes, he did.

Q. Other than saying that this is your answer here, when was the next time that you wrote to the law firm, if ever, and told them of the write-down of $11 million?

A. I don't recall.

Q. Well, do you have any correspondence between you and the law firm, Mr. Ross,

[p.152]

indicating an update on your decision to write off $11 million, yes or no?

A. I don't know if there is anything in writing but there were frequent phone calls updating them on the progress towards getting the issues involved.

Q. Aside from certain phone calls, don't you think, as chief financial officer, there should have been like a sit-down meeting, some emergent meeting with the lawyers and particularly with your investment banker to let them know in July or August of this impending write-down of $11 million?

MR. KAUFMAN: Objection. Lack of foundation, irrelevant, argumentative.

JUDGE FOELAK: Foundation?

Q. Let me ask you, was it customary for you to communicate with the lawyers for W2E?

A. Generally by phone. Often by phone, yes.

Q. What about by e-mail?

A. Generally we spoke by phone.

Q. And generally would you keep minutes or keep a memorandum or a record of what you

[p.153]

talked about?

A. No.

Q. Why not?

A. Just don't. I didn't at the time.

Q. Is that the commonly recognized practice of public companies, that when they speak to the lawyers they don't keep any notes of the conversations?

MR. KAUFMAN: Objection. Foundation, relevance, argumentative.

JUDGE FOELAK: I tend to agree.

Q. Other than this August 19th e-mail and then there is an internal e-mail of October 5, 2009, are you aware of any other documentation that was sent to Mr. Lorenzo concerning the write-down of the $11 million from you?

A. I don't recall specifically anything in writing.

Q. Do you have any records in which you called Mr. Lorenzo and said, "Frank, there is a write-off of $11 million. I just want to make sure that you guys know about this"?

A. Do I have records?

Q. Yes.

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A. I have already answered that. I don't have any records.

Q. Did you ever say that to him?

A. Yes. We had a conversation –

Q. When was –

MR. KAUFMAN: Your Honor, the witness was answering the question and was interrupted. I think it was asked and answered anyway.

JUDGE FOELAK: Let him answer.

Q. I am sorry. Go on.

A. Yes, we had a conversation around mid-September when we got to the point where we had finalized the fact that there was going to be a write-down, a total impairment of that asset.

I spoke with one or both of Frank and/or Gregg Lorenzo on the phone at least once. I don't remember the exact date or time of day, but definitely that was communicated to them.

They were aware that that was the big issue that -- that in addition to payment for services previously rendered were the two big issues of trying to get through the audit.

Q. Do you recall whether you spoke to

[p.155]

Gregg Lorenzo or you spoke to Frank Lorenzo?

A. I don't remember if it was a conference call and they both were on or not but there was a phone call made. I believe Frank was on at a minimum and I don't know whether Gregg was on or not.

Q. Do you know whether he was on or do you recall you think he was on? I am not asking you to guess.

MR. KAUFMAN: Your Honor --

JUDGE FOELAK: Let him answer.

A. I believe Frank was on the call because Frank had been my primary important contact within Charles Vista. I spoke with Frank more frequently than I did Gregg.

Q. And what did you say to him and what did he say to you?

A. I don't recall the specifics of the conversation.

Q. You don't recall the specifics and you don't have any notes of the conversation. Correct?

A. Correct.

Q. And you didn't send any subsequent

[p.156]

e-mail to him confirming the subject of the conversation. Correct?

MR. KAUFMAN: Your Honor, other than the exhibit that we have seen several times?

Q. Other than what we have seen. But even that doesn't say "This is to confirm my conversation with you," does it?

MR. KAUFMAN: Speaks for itself.

Q. Does it, sir?

A. It is as it was written.

MR. HANTMAN: If I can just have a moment, your Honor?

JUDGE FOELAK: Certainly.

(Pause.)

Q. Is there any reason, when you first were discussing the potential write-down of this $11 million asset in July or August, that you did not contact your investment banker?

MR. KAUFMAN: Objection. I don't think the testimony is that he didn't contact them. I think it was that he didn't remember whether he had.

JUDGE FOELAK: I guess the testimony is whatever it is.

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MR. HANTMAN: At the risk of being repetitive, this is an important question.

Q. Do you recall, did you call your investment banker, did you personally call your investment bankers --

A. I don't recall if I did specifically. I am pretty sure I didn't in July. But I did know that Mr. Bohan and Mr. Taylor were both in much more frequent contact with the principals of Charles Vista and was told by Mr. Bohan that they were aware of it -- that was in July when I was just diving into everything that was going on with this company.

Q. Do you know of any reason why -- you think they would have a better recollection of what communications there were with Charles Vista than you?

A. I can't answer for them.

MR. KAUFMAN: Objection.

Q. Hmm?

A. I can't answer for them.

Q. Do you know of any reason why they are not here as witnesses?

MR. KAUFMAN: Objection.

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JUDGE FOELAK: That is not for him to answer. Your objection is sustained.

Q. As you sit here now, wouldn't you agree it would have been in the best interest of the holders of these debentures to have known as early as July or August that there was an intent to write down the $11 million goodwill intangible, yes or no?

MR. KAUFMAN: Objection. Your Honor, we really have to clarify what debentures we are talking about because the 12 percent debentures issued in this case were not sold until October.

JUDGE FOELAK: I think that is his point.

MR. HANTMAN: That is my point. They were sold in October yet in July and August –

JUDGE FOELAK: I think his point is, before putting their money in, wouldn't it have been good for them to know?

MR. HANTMAN: The other point is, to rely on one e-mail to say this man should be disbarred or penalized when there could have been –

MR. KAUFMAN: Your Honor.

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JUDGE FOELAK: That is something for your brief, not a question for this witness.

Q. Did you ever discuss – well, when was the PPM ever amended to reflect write-down of the $11 million?

A. When was it amended?

Q. Yes.

A. It would have been toward latter part of September once the audited financials were confirmed, signed off on by the audit firm.

Q. This would have been at the end of September?

A. The latter part of September.

Q. What were the implications of a write-down of $11 million in intangible goodwill on the debenture holders?

A. What were the implications?

Q. Yes.

A. Well, it was a non-cash write-off of about $11 million. Certainly changed the balance sheet valuation of the company and from an investor's standpoint that number prior to being written down was a perceived value of the technology that had been acquired and was the

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foundation of the technology used in the business.

Q. So what happened between, say, June and July or August which resulted in what was previously supposedly a bona fide asset becoming worth zero?

A. I can only speak from the time I joined the company and started to understand the issues. So anything prior to first week of July 2009 I can't speak to.

There was – there were questions within the company itself about the value of those assets. I asked questions, there were questions internally. That whole

dialogue got into the crux of really what the audit major issue was, was what, if any, value is there to these assets going forward.

Q. Let me apologize, because you did get involved with this situation at a much later period of time. But isn't it a fact that once you did get hired and you took a focus as to what is going on that you even told people at W2E that this was a big problem and that you saw no need to keep this $11 million on the books

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and that it was wrong not to advise the investment banker of what's going on? You were like the white knight? You came in --

MR. KAUFMAN: Objection, your Honor. I don't know how many questions there are here but there are a bunch of them and they are mostly argumentative.

MR. HANTMAN: I will rephrase that.

Q. When you first got wind of what was going on, isn't it a fact, based upon your integrity and your experience, that you told the company that they had an obligation to notify Charles Vista as soon as possible and make a big deal and treat this as important as it was and let them know of the write-down?

A. Yes. I mean, it was an obligation and I was -- had been told that they were aware of it, that they had been aware that there were concerns about the valuation of this in the past.

Q. And you were also told -- let me remind you, you are under oath and your obligation is to tell the truth here. Okay?

You were also told "Listen, let's drag

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this out as long as possible –"

MR. KAUFMAN: Objection. Asked and answered.

Q. "– until the filing so we can get more money to pay bills"?

JUDGE FOELAK: Counsel, haven't you asked that question several times, including the term "gravy train" several times?

MR. HANTMAN: If your Honor recalls that I have, I will defer to your judgment.

Q. When did you first discuss any contingency plan with Charles Vista with respect to the write-down of this asset?

MR. KAUFMAN: Objection to –

Q. Did you ever discuss a contingency plan with Charles Vista?

MR. KAUFMAN: Objection. Vague. What is a contingency plan?

Q. Have you ever heard the words "contingency plan"?

A. I have heard of the words "contingency plan."

Q. What is your understanding of the words "contingency plan"?

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A. It is a plan to do something as a back-up.

Q. So knowing -- when you got involved with the company, knowing that they were cash poor, knowing that things were not going too well, did you have any idea what the result would be on the ability to raise money if the $11 million was written off the books?

A. Did I have any idea?

Q. Yes.

A. I don't recall specifically. I certainly would have relied upon the expertise of the investment banking firm to advise us of that.

Q. Well, did they participate in the meetings in July?

A. Which meetings are you referring to?

Q. The meetings when you started talking about possibly writing off the 11 million.

A. I don't recall -- they were not at any meetings in person with me.

Q. What about in August?

A. I never met in person with anybody from them, so I never had any in-person meetings

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with Charles Vista personally.

Q. Did anyone from your company ever have any personal meetings --

A. Yes.

Q. -- in July, August or September?

A. I believe so, yes.

Q. Who?

A. Mr. Taylor and Mr. Bohan I am pretty sure did.

Q. Is Mr. Taylor a witness?

MR. KAUFMAN: Objection, your Honor. At this point I am going to raise a general objection to where this is going. I think the extent of the witness's knowledge has been established and his knowledge of the facts, well-established. Seems like we are going in circles.

MR. HANTMAN: Your Honor, I am not going to belabor this. I think we have gotten as much as we can from this witness. Thank you.

JUDGE FOELAK: Thank you.

MR. KAUFMAN: Just a couple of questions on redirect, your Honor.

JUDGE FOELAK: Okay.

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MR. KAUFMAN: First of all, Exhibit 13, I think, was not introduced into evidence. We'd just like to offer it. I think it has been adequately authenticated but the witness can testify about it if necessary. This is the memo.

JUDGE FOELAK: The memo that was discussed in cross-examination. Okay. Exhibit 13 is admitted.

(So received in evidence as Division Exhibit 13.)

MR. KAUFMAN: This is sort of another housekeeping matter. I think it is. Exhibit 42, if we can put that up on the screen? It is essentially another version of Exhibit 19. There is one difference. This is the October 5th e-mail that Mr. Brown sent to Mr. Zdanow, Mr. Bohan and Mr. Lorenzo and then it looks like it was forwarded to Gregg Lorenzo by Andre Zdanow. We will offer this into evidence because it is just a clearer version of the same document.

JUDGE FOELAK: Hearing no objection, Exhibit 42 is admitted.

[p.166]

(So received in evidence as Division Exhibit 42.)

MR. KAUFMAN: The only thing I wanted to clarify with the witness, your Honor, a couple of things.

REDIRECT EXAMINATION

BY MR. KAUFMAN:

Q. You were asked some questions about the private placement memorandum for the 12 percent debentures. Do you recall that?

A. Yes.

Q. What was the extent of your personal involvement with respect to the private placement memorandum?

A. More or less as a reviewer of the document. The bulk of the content of it had been developed by the outside legal counsel and a lot of it had been done, I think, prior to my arrival and as I was more focused on the audit, per se. There was work going on on that in the background with legal counsel.

Q. Is it fair to say the PPM was not a significant focus of your job at the time?

A. That is fair to say, yes.

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Q. The 12 percent debenture offering, again, that we talked about before, when did that offering begin?

A. October 1st is when -- it launched after we got current on our filings.

Q. In other words, that is when they were first sold?

A. When they were first sold. Yes.

MR. KAUFMAN: That is all we have, your Honor.

MR. HANTMAN: I just have a little bit on this one exhibit.

JUDGE FOELAK: Okay. Recross.

RECROSS-EXAMINATION

BY MR. HANTMAN:

Q. If you can look at Exhibit 13? Do you see it?

A. Yes.

Q. It says "Memo to file." Correct?

A. Yes.

Q. Does it say who prepared this memo?

A. This does not.

Q. Do you know who prepared it?

A. The bulk of it was prepared by me.

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Q. Is this the most comprehensive explanation as to why the $11 million is being written off that you are aware of?

MR. KAUFMAN: Your Honor, this is beyond the scope of the redirect.

JUDGE FOELAK: That is okay. Go ahead and answer.

A. I am not aware of any other documents outside of this. This was intended to be a summary of a variety of conversations and basically was an opportunity for me to kind of pull everything together that I had gathered during my fact-finding once I got on board with the company.

Q. And it was your decision that it was more prudent, before you shared this with Charles Vista, you wanted to share this with your colleagues at W2E. Correct?

A. Well, not only with my colleagues within the company but with the accounting firm as well.

Q. Do you know why -- was this ever sent to Charles Vista, this memo itself?

MR. KAUFMAN: Asked and answered.

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A. I don't recall.

Q. Was the write-down of the potential $11 million ever disclosed in writing to the investors?

MR. KAUFMAN: Objection. We are back at, I think, the original cross.

JUDGE FOELAK: I think we are.

Q. What, if anything, happened as a result of this memo?

MR. KAUFMAN: Objection. Vague and, again, beyond the scope.

MR. HANTMAN: Your Honor, apparently this was not put into evidence and then Mr. Kaufman put it into evidence, which I have no problem with. After his direct he put it into evidence. I understand it might have been inadvertent but I have an obligation or the right to cross-examine him on something that is evidence in the case.

MR. KAUFMAN: We ask that the question be rephrased in a way that everyone can understand it.

JUDGE FOELAK: Okay. Sounds good.

Q. Did you get any response to this memo

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that you prepared for the file on September 16, 2009?

A. Did I get any response?

Q. Yes.

A. From whom?

Q. From anyone.

A. I don't recall. I am sure the audit firm probably had some maybe questions or things they wanted to further clarify. But I don't recall if I had specific responses.

Q. Do you have any memorandum indicating that you had any responses?

A. No.

Q. Do you have any memorandum indicating that you ever sent this to Charles Vista?

A. Do I have a memorandum?

Q. Yes.

A. That I sent this to them? No.

Q. Do you have any proof that this was ever sent to Charles Vista or to Francis Lorenzo?

MR. KAUFMAN: Objection. The witness has testified that he doesn't recall sending it to Charles Vista.

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MR. HANTMAN: He doesn't recall.

Q. But do you have any indication in the memo that it was sent to Charles Vista?

A. I don't recall.

Q. Do you know of any reason why this wouldn't be sent to your investment banker?

A. I don't recall whether it was or was not.

Q. As you sit here now, wouldn't you agree that something this important, which is a summary of your findings on a $11 million write-down should be sent to your investment banker?

A. Again, I believe it was communicated to them verbally. I don't recall specifically if this in-depth write-up was provided to them. I just don't recall.

MR. HANTMAN: Thank you.

MR. KAUFMAN: Nothing further, your Honor.

JUDGE FOELAK: Okay. Thank you for your testimony, Mr. Brown. You may step down.

THE WITNESS: Thanks.

MR. KAUFMAN: Your Honor, the Division

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is calling, by telephone, William Rothe.

(Speakerphone call placed.)

MR. KAUFMAN: Mr. Rothe, this is Jack Kaufman. We are in the courtroom.

JUDGE FOELAK: This is Judge Foelak. I understand you are in California.

MR. ROTHE: Yes.

JUDGE FOELAK: I will put you under oath.

Whereupon,

WILLIAM ROTHE,

having been first duly sworn/affirmed, was examined and testified as follows:

JUDGE FOELAK: Please proceed.

DIRECT EXAMINATION

BY MR. KAUFMAN:

Q. Mr. Rothe, this is Jack Kaufman. Can you, please, state and spell your full name for the record?

A. William Rothe, spelled R-O-T-H-E.

Q. Where do you reside, sir?

A. Santa Rosa, California.

Q. Is that where you are now?

A. Yes.

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Q. How old are you, sir?

A. 67.

Q. Are you currently employed?

A. I work for myself.

Q. In what sort of capacity?

A. I am a private lender to real estate and an investor in real estate and I grow grapes.

Q. Are you familiar with an entity called Charles Vista?

A. Yes.

Q. How do you know Charles Vista?

A. I brought a hundred shares of stock through them some years ago.

Q. Do you remember what year that was?

A. I think it was 2008 or it would have been early 2009.

Q. So is it fair to say that you were a customer of Charles Vista?

A. I was a customer. Yes.

Q. Did you have an account there?

A. Yes.

Q. During what period of time were you a customer at Charles Vista?

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A. I was a customer from the time I bought the stock, which would have been again probably early 2009, and until about two months ago when I sold the stock.

Q. And how long did you hold a brokerage account there?

A. For that period of time from 2009 until maybe two months ago.

Q. Do you have a document that has been marked as Exhibit 49?

A. Yes.

Q. And the first page of that says "Premier account statement for Charles Vista, William Rothe." Do you have that in front of you?

A. Yes.

Q. Can you just tell us what that document is?

A. It is a period ending September 30, 2009 showing the portfolio value as of that date.

Q. Is this your Charles Vista account statement for that period?

A. Yes, it is.

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MR. KAUFMAN: The Division offers Exhibit 49.

JUDGE FOELAK: Hearing no objection, Exhibit 49 is admitted. But, counsel, you should take out his home address and any other type of personally identifying information.

MR. KAUFMAN: Objection. We will redact that before we submit it to the Court.

(So received in evidence as Division Exhibit 49.)

Q. Mr. Rothe, did you receive any other account statements other than this?

A. I did. I think I received one a month.

Q. Both before and after September 2009?

A. I would have received them immediately after I purchased the stock and then through until I sold the stock.

Q. In other words, you received account statements up until relatively recently?

A. Yes.

Q. Did you have an individual assigned as a broker to you as Charles Vista?

A. There was a name on my account, and I

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do not remember or do not recall the person with whom I placed the order and do not recall anybody I talked with after that.

Q. Did you understand that you had a personal broker there or not?

A. They had a name on there so if I needed – if I had any questions I had a name and a number I can call; yes.

Q. This document says Jason Cabrerra. Is that the person you are referring to?

A. That would be who I would call on my account, yes. I don't know if I ever talked to Mr. Cabrerra or not.

Q. Let me ask you to look at -- do you have another document that has been marked Exhibit 34?

A. Yes.

Q. I just want to refer to the third and fourth pages of that document.

A. Yes.

Q. This appears to be an e-mail from Francis Lorenzo dated October 14th to a W.S. Rothe at Sbcglobal.net. October 14, 2009. Was that your e-mail address at the time, Mr. Rothe?

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A. Yes, and it still is.

Q. Did you receive this e-mail –

A. Yes.

Q. Sorry. Let me ask the full question. Did you receive the e-mail on October 14, 2009?

A. I am presuming I did, yes.

Q. Did you ever open the e-mail?

A. Yes.

Q. When did you open it?

A. On the 16th.

Q. Of October, 2009?

A. Yes.

Q. How do you know that?

A. I was on my way to live on the other side of the world and I was clearing my spam account in which this e-mail arrived and I wanted to read it at a later date so I forwarded it to myself in my in-box on the

16th and then presumably read it at some time later, living on the other side of the world.

MR. KAUFMAN: The Division offers Exhibit 34.

JUDGE FOELAK: Exhibit 34 is admitted.

(So received in evidence

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as Division Exhibit 34.)

Q. I can't remember -- I am not sure if I heard your answer but did you ever read this e-mail?

A. Yes. I am presuming I did.

Q. When did you read it?

A. It would probably have been three or four days after the 16th.

Q. The e-mail refers to 12 percent debenture. Did you ever invest in that?

A. No.

Q. Did you ever invest in Waste2Energy at all?

A. No.

MR. KAUFMAN: A moment, your Honor?

JUDGE FOELAK: Yes.

(Pause.)

MR. KAUFMAN: No further questions at this time, your Honor.

JUDGE FOELAK: Mr. Hantman?

CROSS-EXAMINATION

BY MR. HANTMAN:

Q. Mr. Rothe, have you ever met Francis Lorenzo?

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A. No.

Q. Have you ever spoken to Mr. Lorenzo?

A. I do not recall.

Q. Have you ever heard of Francis Lorenzo?

A. Yes.

Q. From whom?

A. Through Charles Vista.

Q. When was that?

A. Well, I think that Francis Lorenzo is one of the officers or one of the principals of Charles Vista.

Q. And who told you that?

A. Well, it is on his e-mail on October 14th. Francis Lorenzo, vice president investment banking.

Q. Aside from this e-mail, was there anything else he ever sent you?

A. No, that I can think of. I received several other e-mails on W2E, Waste2Energy, but they did not -- no, they didn't come from Francis Lorenzo.

Q. And as a result of retrieving this from your spam, what, if anything, did do?

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A. I am sorry. Can you repeat that a little louder, please?

Q. After you retrieved this from your spam file what, if anything, did you do in response to this e-mail?

A. Nothing.

Q. And you didn't lose any money. Correct?

A. Can you repeat that again, please?

Q. You never invested as a result of this e-mail; correct?

A. No, I did not.

Q. And you never called anybody at Charles Vista to discuss this e-mail, did you?

A. No.

MR. HANTMAN: No further questions.

MR. KAUFMAN: That is it, your Honor.

JUDGE FOELAK: Okay. Thank you for your testimony, Mr. Rothe, and we are going to ring off now.

MR. KAUFMAN: Thank you, Mr. Rothe.

THE WITNESS: Thank you.

(Phone call ended.)

MR. JANGHORBANI: The Division calls

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Francis Lorenzo.

Whereupon,

FRANCIS LORENZO,

having been first duly sworn/affirmed, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. JANGHORBANI:

Q. Good afternoon. Could you, please, state and spell your full name for the record?

A. Francis Lorenzo -- V. Lorenzo, F-R-A-N-C-I-S.

Q. V for Vincent?

A. Vincent. L-O-R-E-N-Z-O.

Q. How old are you, sir?

A. 52.

Q. You live in Westwood, New Jersey. Correct?

A. Yes, I do.

Q. You worked at Charles Vista from February 2009 to February 2010. Correct?

A. Yes.

Q. You were Charles Vista's director of investment banking. Correct?

A. Yes, I was.

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Q. Charles Vista was a brokerage firm. Correct?

A. Yes, it was.

Q. And an investment bank. Correct?

A. Yes, it was.

Q. And Charles Vista's role as an investment bank was to raise money for its clients. Correct?

A. One of them.

Q. Generally that is what it did for its investment banking clients; it helped them raise money. Correct?

A. The ones I was working on, yes, that's what they did.

Q. And Charles Vista's investment banking clients, just so we're clear, those were companies. Correct?

A. Correct.

Q. Now, part of your job at Charles Vista was to do due diligence on investment banking clients. Correct?

A. Prepare due diligence.

Q. And part of your job was to review investment banking clients' financial

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statements. Correct?

A. Yes, it was.

Q. You understood that that was one of the requirements of your job. Correct?

A. Yes, it was.

Q. Now, if an investment banking client was a public company it was also part of your job to review the company's public files with the SEC. Correct?

A. Yes, it was.

Q. And part of your job was to look at your client's assets and liabilities. Correct?

A. Correct.

Q. In other words, the balance sheet. Correct?

A. Correct.

Q. And part of your job was to prepare offering documents. Correct?

A. Assist with preparation, yes.

Q. But you had a hand in preparing offering documents to your clients. Correct?

A. For the corporate investment banking clients, yes.

Q. Thank you. I am saying clients as

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shorthand for investment banking clients but thank you for reminding me of that.

And another part of your job was to make sure that your investment banking clients had all material disclosures in place. Correct?

A. Absolutely.

Q. Now, back in 2009 you were a registered representative. Correct?

A. Yes.

Q. Of Charles Vista; right?

A. Correct.

Q. And you had a Series 7 license?

A. Yes, I did.

Q. You still have a Series 7?

A. Yes, I do.

Q. Now, you had experience in investment banking before you joined Charles Vista. Correct?

A. Yes, I did.

Q. In fact, you had vast experience; right?

A. Vast? Yeah, I guess. I guess it is a matter of interpretation. Yeah, I'd say that's accurate.

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Q. And starting in 1986 you worked at a firm called Spear, Leeds & Kellogg. Correct?

A. Correct.

Q. When did you work -- from 1986 until when?

A. Until the crash in '87.

Q. '86 to '87. And you were an arbitrage trader. Correct?

A. On the American Stock Exchange, yes.

Q. You were an arbitrage trader on the American Stock Exchange?

A. Correct.

Q. I was just making sure I heard you.

In January '97 you formed something called Loren investment group. Correct?

A. Correct.

Q. You worked there until February of '01?

A. That sounds accurate. It is going back a ways but, yes.

Q. That sounds right?

A. Yes.

Q. At Loren you advised companies and how to go public. Right?

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A. Correct.

Q. And how to raise capital. Correct?

A. Correct.

Q. Raising capital, that means raising money; right?

A. Yes.

Q. Capital is money? You have to answer audibly.

A. Yes, that is correct.

Q. Now, in 2001, you founded a company called OTC Solutions LLC.

A. That is correct, yes.

Q. The "OTC" stands for over the counter?

A. Over the counter, yes.

Q. You were the CEO of that company?

A. Yes.

Q. That is chief executive officer?

A. Correct.

Q. And OTC's business was to assist microcap companies with capital formation; correct?

A. Among others things, yes.

Q. That was parts of its business. Correct?

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A. Correct.

Q. Again, when we talk about capital formation, you understand that means raising money. Correct?

A. That is correct.

Q. Another part of OTC's business was to help companies with public financing. Correct?

A. Yes.

Q. That means selling securities to the public. Correct?

A. I couldn't sell securities. I'd get –

Q. That means that the company – the client of OTC would sell securities to the public?

A. The client of the OTC.

Q. That is what public financing is; correct?

A. Yes. I thought you meant me.

Q. In February 2007, you went to work for a company called Mercer Capital?

A. That is correct.

Q. And Mercer was a registered broker-dealer?

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A. Correct.

Q. And you were the investment banker for Mercer. Correct?

A. Yes, I was.

Q. You left Mercer at the end of 2007. Correct?

A. Yes.

Q. December?

A. November, December, something like that, yes.

MR. JANGHORBANI: Mr. Chan, can I ask you to put Division Exhibit 25 on the screen?

Q. Can you see that, Mr. Lorenzo?

A. Not yet -- I see it.

Q. This is 25. We have all the same documents in hard copy in front of you.

This document says "U-4 employment form, individual name Lorenzo, Francis V." You see that?

A. Yes, I do.

Q. This appears to be an employment history for you. Correct?

A. Correct.

Q. And it appears to be accurate.

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Correct?

A. Yes.

MR. JANGHORBANI: I move the admission of Division Exhibit 25, your Honor.

JUDGE FOELAK: Division Exhibit 25 is admitted.

(So received in evidence as Division Exhibit 25.)

Q. You left Mercer, I believe you said, in December 2007. Do I have that right?

A. Yes. I am cut off at John Thomas here. I can't see Mercer but --

MR. JANGHORBANI: Mr. Chan --

A. Oh, there it is. I got it.

MR. JANGHORBANI: And you can take the document down, Mr. Chan.

Q. Now, in February 2008, you started working at John Thomas Financial; right?

A. Yes, I did.

Q. That is also a broker?

A. Yes.

Q. And an investment bank?

A. Yes.

Q. You were there their investment

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banker; right?

A. One of them, yes.

Q. And you left in December '08. Correct?

A. I think it was November but it could be December.

Q. That was to join Charles Vista?

A. Well, no.

Q. Withdrawn. You joined Charles Vista in February '09. Correct?

A. Correct.

Q. You are familiar with a company called Waste2Energy Holdings, Inc. Correct?

A. Yes, I am.

Q. That was an alternative energy company?

A. Correct.

Q. And its business was it developed technology to burn waste in order to turn that waste into energy. Correct?

A. That is correct.

Q. Now, you first heard of Waste2Energy when you were an investment banker at Mercer. Right?

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A. Yes, I did.

Q. In fact, Mercer helped Waste2Energy sell $6 million in shares. Correct?

A. That is correct.

Q. And Waste2Energy became an investment banking client of Charles Vista's. Correct?

A. Yes, it was.

Q. That was in approximately March of 2009?

A. Give or take, that sounds accurate.

Q. March or April 2009?

A. Something like that.

Q. And Charles Vista helped Waste2Energy sell securities. Correct?

A. That is correct.

Q. Charles Vista helped Waste2Energy sell equity; correct?

A. Yes.

Q. About 1.2 million worth?

A. I thought it was less than that but it's been a while. I know they did an equity round at the time they did the reverse merger but I didn't think it was 1.2.

Q. Charles Vista helped Waste2Energy sell

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2 and a half million dollars in short-term debt. Correct?

A. That is correct.

MR. JANGHORBANI: Your Honor, I would like to read -- well, let me withdraw that.

Q. Mr. Lorenzo, can I ask you to turn to the binder labeled "Testimony transcripts"? It is the skinny binder at the bottom.

A. Got it. Yes.

Q. Can I ask you to turn to page 205? You see there are four numbered pages per each actual page?

Well, before I do that, you recall giving testimony to the staff of the SEC on November 12, 2009?

A. November 12th?

Q. Yes, 2009.

A. Yes.

Q. And you were under oath during that testimony. Correct?

A. Yes, I was.

Q. And you told the truth during that testimony. Correct?

A. Yes, I did.

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MR. JANGHORBANI: Your Honor, I would like to read an admission.

MR. HANTMAN: Your Honor, I object. I think the proper format would be to ask him a question and if his answer is different, then you point out the inconsistency in the deposition testimony.

MR. JANGHORBANI: Your Honor, I am not offering it for impeachment, although I could. I am offering it as an admission against party opponent under Rule 802 of the Federal Rules. It is not hearsay. It's an exception from hearsay and I am allowed simply to read it.

JUDGE FOELAK: The Commission has ruled that excerpts from investigative testi.nony can be admitted. Plus you could also use it for impeachment.

MR. HANTMAN: As long as it is not out of context because I am not sure what he is --

JUDGE FOELAK: I understand what you mean.

MR. JANGHORBANI: It is page 205.

JUDGE FOELAK: Mr. Hantman was referring to the idea that you could pluck a

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sentence standing by itself out of context and it would mean something completely different.

MR. JANGHORBANI: I had planned, your Honor, to read a passage of full questions and full

answers. Page 205, lines 7 to 24. May I read, your Honor?

THE WITNESS: Lines 70?

MR. JANGHORBANI: Page 205, line 7 to 24.

JUDGE FOELAK: Line 7, not 70.

THE WITNESS: Okay.

MR. JANGHORBANI: May I read, your Honor?

JUDGE FOELAK: Okay, you can read it.

MR. JANGHORBANI: "Question. How much money was raised?

"Answer: I have to double check. I believe it is 3.5, 4 million, give or take. No, no, I take that back. I am sorry. My mistake. 1.2 million worth of equity was raised. About 2.5 million of short-term notes were raised right after the equity round."

Q. Did I read that correctly, Mr. Lorenzo?

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A. Yes, you did.

Q. Now, Waste2Energy was Charles Vista's biggest client; right?

A. Yes, it was.

Q. And while you were at Charles Vista you worked exclusively on Waste2Energy. Correct?

A. No. Well, up until October when China Baicaotang came in. September, October there was a China deal that came in.

Q. But China Baicaotang, Charles Vista wasn't the banker on that deal, was it?

A. We were the selling group on the deal.

Q. For investment banking clients isn't it the case that your sole and exclusive investment banking client, you personally while you worked at Charles Vista, was Waste2Energy?

A. Well, I founded -- I brought China Baicaotang into Charles Vista and worked on the memorandums with Larry Nussbaum and ND Capital. As far as proprietary client, it was Waste2Energy. Charles Vista was selling China Baicaotang in September and October.

Q. You gave testimony to the Commission

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on July 26, 2012. Correct?

A. July 26, 2010? Okay.

Q. Is that correct?

A. Yes, I did.

Q. And you were under oath during that proceeding. Correct?

A. Okay.

Q. I'm asking you. Is that correct?

A. Yes.

Q. And you answered questions truthfully. Is that correct?

A. Yes, I did.

MR. JANGHORBANI: Your Honor, I would like to read from page 18, line 21 to page 19, line 3. May I read, your Honor?

JUDGE FOELAK: Let's wait until Mr. Hantman gets there.

MR. HANTMAN: Thank you, your Honor.

JUDGE FOELAK: Go ahead.

MR. JANGHORBANI: "Question: Did you continue to review public filings of a company after it hired Charles Vista?

"Answer: Well, I worked fully and exclusively on Waste2Energy. So there was a

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China company called China Baicaotang but we weren't the banker on that deal. Charles Vista, when I was there, when you mention companies, there wasn't any companies. It was just Waste2Energy."

Q. Did I read that correctly, Mr. Lorenzo?

A. Yes, you did.

Q. Okay. And you did due diligence to Waste2Energy. Correct?

A. Well, I think it depends on how you define due diligence but I prepare a questionnaire. I put the documents -- I answered the questionnaire with the company.

Q. And you consider that due diligence. Correct?

A. Yes.

Q. And you reviewed Waste2Energy's SEC filings. Right?

A. Correct.

Q. That was part of your job as director of investment banking. Correct?

A. Yes, it was.

Q. In fact, you reviewed Waste2Energy's

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filings immediately after they were filed. Isn't that right?

A. I reviewed them, yes. Looked through them, yes.

Q. You reviewed them within 48 hours of them being filed. That was your practice, wasn't it?

A. Yeah.

Q. Is that a yes?

A. Yes, that's correct.

Q. During your time at Charles Vista Waste2Energy was start-up company. Correct?

A. Yes, I guess that would be accurate.

Q. It was an early stage company?

A. Early stage. Yes.

Q. It wasn't profitable; right?

A. No.

Q. In fact, its financial situation wasn't good at all, was it?

A. It wasn't.

Q. Its financial well-being was horrible, wasn't it?

A. That is correct.

Q. And you certainly understood that by

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September 1st of 2009, didn't you?

A. I certainly knew that by September 1st? Well, their financial situation was horrible from the beginning, yes, so that would be accurate.

Q. And, in fact, during your time at Charles Vista, Waste2Energy's technology didn't really work, did it?

A. No. They were waiting on a part.

Q. Okay.

A. Yes.

Q. While you were at Charles Vista it's fair to say, isn't it, that its technology was able to incinerate waste but it wasn't able to turn it into energy?

A. That was my understanding.

Q. So it could do the waste but not the energy?

A. That was my understanding.

Q. Waste2Energy filed a Form 8-K with unaudited financial statements in June 2009. Correct?

A. Early June, yes, the Maven -- the one that says Maven Media on it?

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Q. In early June 2009. Is that correct?

A. I think so, yes.

MR. JANGHORBANI: Mr. Chan, can you pull up Division Exhibit 15? This is already in evidence, your Honor.

JUDGE FOELAK: Yes.

Q. Mr. Lorenzo, is that up on your screen? We have looked at this document earlier with Mr. Brown. You see it says "Form 8-K, Maven Media Holdings Inc., May 28, 2009." You see that?

A. Yes, I do.

Q. Maven Media was just Waste2Energy's prior name. Correct?

A. Well, Maven Media was the name of the shell that Waste2Energy did an RTO with.

Q. You mean a reverse merger?

A. Yes.

Q. And when it did a reverse merger, Maven Media changed its name to Waste2Energy Holdings Inc. Correct?

A. Correct.

Q. The merger occurred in late May 2009. Correct?

[p.201]

A. That is correct.

Q. Could I ask you to turn to page 61? You see this document is signed June 3, 2009?

A. Yes, I do.

Q. So it is fair to say that Waste2Energy filed this 8-K on June 3, 2009. Correct?

A. That is correct.

Q. And you saw this 8-K in early June 2009. Correct?

A. Yes.

Q. Right around June 3rd; right?

A. Correct.

MR. JANGHORBANI: Mr. Chan, could you turn to page 63, please? Just the first half of the page, Mr. Chan? Thank you.

Q. You see it says "Waste2Energy Inc." and "Subsidiaries consolidated balance sheet"?

A. Yes, I do.

Q. You see there is a column that says "December 31, 2008, unaudited"?

A. Yes.

Q. So this is the balance sheet as of December 31, 2008?

A. Yes.

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Q. And it was unaudited. Correct?

A. Yes, that is correct.

Q. You understand by "unaudited" that meant these financials had not been signed off on by a qualified auditor. Correct?

A. Yes.

Q. And you understood then that no auditor was making any representation about these numbers. Correct?

A. I don't know if I can a hundred percent answer that correctly because there was conversations with Marcum Kliegman that the audit was looking good at the time.

Q. But these numbers weren't audited. Correct?

A. Yes.

Q. So just these numbers on this balance sheet, you understood that no auditor was making any representation about these December 31, 2008 unaudited numbers. Correct?

A. Yes, that is correct.

Q. At the time it was significant to you, wasn't it, that these financials weren't audited?

[p.203]

A. Yeah.

Q. Did you say yes, sir?

A. Yes, I did.

Q. And that is because an audit gives comfort that Waste2Energy's financials are accurate. Correct?

A. Correct.

Q. In fact, without an audit there is way too much risk for investors. Correct?

A. That sounds accurate.

Q. So that is a yes?

A. Yes.

Q. I have already directed you to this but you see it says December 31, 2008. Right?

A. Mm-hmm.

Q. These numbers were six months old when you first saw them. Correct?

A. These numbers were six months old? Yes, that is correct.

Q. Now, you see "Total assets"? You see a row that says "Total assets" and then it says $13,987,764?

A. Yes.

Q. You understood that is the total

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assets being reported of Waste2Energy?

A. Yes.

Q. And then you see a couple lines up there is a line that says "Intangibles net"?

A. Yes.

Q. Next to that it says "$10,038,558"?

A. Yes.

Q. That 10 million in intangible assets that was Waste2Energy's intellectual property. Correct?

A. I believe so.

Q. That is what you understood. Correct?

A. Yes.

Q. And by far Waste2Energy's biggest asset. Correct?

A. Absolutely.

Q. Now, you had concerns at the time back in June 2009, didn't you, about whether this asset was really worth $10 million?

A. Yeah.

Q. Yeah, and that is because you thought it was a dead asset.

I am sorry. Did you say yes?

A. Yes.

[p.205]

Q. That was because you thought it was a dead asset. Correct?

A. I may have said dead but I know that it is going to be discounted. Intellectual properties are hugely discounted so -- upon liquidation. So I may have used the word dead in my testimony but an intangible asset is questionable. Put it that way.

Q. At a minimum you understood that it was illiquid. Correct?

A. Yes.

Q. You didn't believe that Waste2Energy would be able to get $10 million for this asset. Is that correct?

A. Yes, that's correct.

Q. That is a no?

A. That is a no.

Q. In fact, Waste2Energy would be lucky to get a million dollars for this asset. Correct?

A. I believe I testified to that, something like that, yes.

Q. So that is what you believed. Correct?

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A. Correct.

Q. And you referred to this asset as a dead asset, didn't you?

A. It is going back a ways. I may have used the word dead.

MR. JANGHORBANI: Your Honor, I would like to read another admission from the July 26, 2012

transcript, page 56. I will give everyone a second to catch up.

A. What page was that?

Q. Page 56?

A. Dead asset. Okay.

MR. JANGHORBANI: Starting at line 6, your Honor, and going to line 14. May I read, your Honor?

JUDGE FOELAK: Is Mr. Hantman there?

MR. HANTMAN: I am not sure where you are.

MR. JANGHORBANI: The July 6th testimony.

MR. HANTMAN: Thank you.

MR. JANGHORBANI: May I read, your Honor?

JUDGE FOELAK: Yes.

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MR. JANGHORBANI: "Question: I think what Mr. Osnato may be getting at was there is something particular about the asset that prompted you to say that?

"Answer: Yes. It was a dead asset.

"Question: What do you mean by dead asset?

"Answer: Illiquid. And upon liquidation there is no way you are going to get even close to $10 million. So if there was a liquidation you are lucky you can get a million dollars for that asset."

Q. Did I read that correctly, Mr. Lorenzo?

A. Yes, you did.

Q. In fact, you didn't consider this $10 million to be a significant source of collateral. That's fair to say?

A. I'd say that's accurate.

Q. You didn't think it was a tangible source of collateral against debenture. Isn't that fair to say?

A. I think that's fair to say.

Q. Now, we have just looked at the

[p.208]

financials, the unaudited December 31st financials. You understood that Waste2Energy's financials were in the process of being audited. Correct?

A. Yes.

Q. And you knew that, that that process was going on in the summer of 2009. Correct?

A. Yes.

Q. You certainly understood it was going on by August 2009. Correct?

A. Yes.

Q. And Waste2Energy was having an audit done for the purpose of filing a Form 10-Q. Correct?

A. A Form 10-Q? Yes.

Q. You were aware of that by August 2009 as well. Correct?

A. Yes.

MR. JANGHORBANI: Mr. Chan, can you pull up Exhibit 30? That is in evidence already, your Honor.

Q. Mr. Lorenzo, do you have that on your screen?

A. I do.

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Q. This appears to be an e-mail from Francis Lorenzo to Craig Brown dated August 19, 2009. Is that correct?

A. That is correct.

Q. That is your e-mail address on top; right?

A. Yes.

Q. That is Florenzo@charlesvista.com. Is that correct?

A. That is correct.

Q. You see two e-mails down is an e-mail from Craig Brown dated August 19th at 4:37 p.m. Do you see that?

A. Yes, I do.

Q. You see Mr. Brown wrote, "We are continuing to work on 3/31 numbers and hope to get the audit going this week and be in a position to file audited statements for March 31st in the next two weeks."

Do you see that?

A. Yes, I do.

Q. And that is the audit we have just been discussing. Correct?

A. Yes.

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Q. So you knew the audit hadn't been completed by August 19th. Correct?

A. That is correct.

Q. And you see that Mr. Brown then writes, "We expect to be able to get a 10-Q done and filed in short order after the 3/31 numbers are filed with the SEC." You see that?

A. Yes, I do.

Q. That is the same 10-Q we were just talking about. Correct?

A. Correct.

Q. You understood Waste2Energy was preparing an audit in order to file it with the 10-Q?

A. Correct.

Q. You knew, didn't you, that Waste2Energy was late in getting its audit done?

A. Yes.

Q. That is what this e-mail is telling you; right?

A. Right.

Q. In fact, you respond to Mr. Brown's information, don't you?

A. Yes.

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Q. You write "Thanks for the update and the great work." Right?

A. That's correct.

Q. Now, at the same time the audit was going on, Waste2Energy was working on a private placement memorandum for a debenture offering. Correct?

A. That is correct.

Q. Can I ask you to turn to Division Exhibit 3? It may be easier to look at it in binder initially at least.

A. Got it.

Q. You have that in front of you, sir?

A. Yes, I do.

Q. This is the PPM. Right?

A. This is the September 9th PPM.

Q. So this is a private placement memorandum for Waste2Energy. Correct?

A. Yes, it is.

Q. And it says "Private offering memorandum" on top but private offering memorandum is just another way of saying private placement memorandum?

A. That is correct.

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Q. Okay. And you see on the second page it is dated September 9, 2009?

A. Yes.

Q. All right.

And this private placement memorandum is offering 12 percent convertible debentures. Correct?

A. Yes, correct.

Q. The maximum offering of $15 million?

A. Yes.

Q. And Charles Vista was the exclusive placement agent for this deal?

A. Yes, that.

Q. Can you keep your voice up, sir? I am sorry. I am having trouble hearing you.

A. No worries.

Q. You prepared this private placement memorandum, didn't you?

A. Yes.

Q. In fact, you communicated with Waste2Energy about drafts of this document; right?

A. Yes, I did.

MR. JANGHORBANI: Your Honor, I would

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like to offer Division 3 in evidence.

JUDGE FOELAK: Admitted.

(So received in evidence as Division Exhibit 3.)

Q. And you suggested changes to the PPM. Correct?

A. I guess so.

Q. Now, this is the PPM that was used for the same 12 percent offering that Craig Brown testified about this morning. Correct?

A. I believe so, yes.

Q. You don't have any reason to believe that is not the case?

A. That is correct.

Q. I am sorry. I sort of double-backed a little. You suggested changes to drafts of this PPM. Right?

A. Probably. I mean, I don't know if it was this one or the one beforehand, but, yes, I remember that one e-mail, a couple of changes requesting.

Q. Can I ask you to turn to Division Exhibit 17?

A. 17?

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Q. 17.

A. Got it.

Q. You see this is an e-mail from Francis Lorenzo to David Manno copying a number of people including Craig Brown? Do you see that?

A. Yes, I see.

Q. And you sent this e-mail, didn't you, on August 26, 2009. Correct?

A. Yes, I did.

Q. And the subject line, you see it reads "CV changes edits to the PPM." Correct?

A. Yes.

Q. That is the PPM I just showed you, Exhibit 3?

A. Exhibit 3. Yes.

Q. This subject line, this means that Charles Vista is suggesting changes to a draft of the private placement memorandum. Correct?

A. Correct.

Q. And you were providing those edits?

A. Yes.

Q. And one of the changes that you were suggesting was to include the $10 million intangible asset in the private placement

[p.215]

memorandum. Correct?

A. Provided it was legal to put it in there.

Q. But that is what you were suggesting, yes?

A. Yes. If it was legal, put it in.

MR. JANGHORBANI: Can I ask you to turn to page 3, Mr. Chan?

Q. Do you see at the very bottom you write "We want to mention that the company has IP and intangibles valued at $10,038,558."

A. Correct.

Q. Right? So you got that number from the June 3rd 8-K?

A. Yes, that is correct.

Q. And you were asking if Charles Vista would include that number in the private placement memorandum. Correct?

A. Well, if the lawyers and the auditors approved it, you know, wouldn't we'd want them to –

Q. You wanted to mention it. Correct?

A. Provided that it was allowed to be mentioned.

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Q. You wanted to include it in the private placement memorandum because you thought it was a material number; correct?

A. Based on conversations with the company and with Peter Bohan it was a material number.

Q. You thought it was material. Correct?

A. Not on a liquidation value basis.

MR. JANGHORBANI: Your Honor, I would like to read another admission from the July 26, 2012 testimony, page 83; lines 14 to 17.

May I read, your Honor?

JUDGE FOELAK: Mr. Hantman?

MR. HANTMAN: I am okay.

JUDGE FOELAK: Go ahead.

MR. JANGHORBANI: "Question: So I take it that you were asking Waste2Energy if they could put that number in the private placement memo.

"Answer: Yes, I thought that was material."

Q. Did I read that correctly, Mr. Lorenzo?

A. On page 83?

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Q. 82.

JUDGE FOELAK: Oh.

THE WITNESS: I thought you said 83.

MR. JANGHORBANI: I may have misspoke. I apologize.

THE WITNESS: I am sorry. What was it, sir?

MR. JANGHORBANI: Let me try again. I apologize for that.

Q. Page 82, line 14 to 17: "Question: And so I take it that you were asking Waste2Energy if they could put that number in the private placement memo.

"Answer: Yes. I thought that was material."

Did I read that correctly, sir?

A. Yes, you did.

MR. JANGHORBANI: Your Honor, I move Division Exhibit 17 into evidence.

JUDGE FOELAK: Exhibit 17 is admitted.

(So received in evidence as Division Exhibit 17.)

Q. Mr. Lorenzo, you see on Exhibit 17, which is up on your screen, you see in the

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parentheses it says "Valued on the company's audited financial statement"?

A. Yes, I see that.

Q. The June 3rd 8-K wasn't audited. We just talked about that; right?

A. Correct.

Q. And you understood that; correct?

A. If I continue to read my testimony on page 83 when we address that it says "Is it clear you had made a mistake" and --

Q. Could you, please, put your testimony aside, sir. I am asking you a question.

A. Okay.

Q. No one ever told you that the June 3rd 8-K had ever been audited. Correct?

A. That is correct.

Q. You understood it wasn't audited. Correct?

A. Yes.

Q. Now, this request here, this request to mention the 10 million, Waste2Energy never responded to that request. Correct?

A. I don't remember that they did.

Q. You don't recall ever receiving a

[p.219]

response. Correct?

A. No, I don't recall receiving a response.

Q. And you sent this e-mail on August 26, 2009. Now, by a week later, you really weren't sure what this intangible asset was worth; isn't that fair to say?

A. In a week later – what was the date you mentioned?

Q. Well, you sent Exhibit 17 on August 26th. By a week after that, you weren't sure what the intangible asset was worth. Isn't that true?

A. Yes. That is true. Nobody informed me on what it was worth based on the audit.

Q. Can I ask you to turn to Exhibit 18. Do you see that, Mr. Lorenzo?

A. Yes.

Q. That is an e-mail from you to Peter Bohan and Craig Brown. Correct?

A. Yes.

Q. On September 1, 2009. Correct?

A. Yes.

MR. JANGHORBANI: Your Honor, I move

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Exhibit 18 into evidence.

JUDGE FOELAK: Exhibit 18 is admitted.

(So received in evidence as Division Exhibit 18.)

Q. You sent this about a week after Exhibit 17. Right?

A. Okay.

Q. Is that a yes?

A. Yes.

Q. You see the subject is "CV changes."

A. Yes.

Q. That means Charles Vista's changes to the PPM?

A. Correct.

Q. That is the one we have been talking about in Exhibit 3?

A. Yes.

Q. Now, you see on point 4, you see it says "IP intangibles as an asset valued at," dollar symbol – then there is a blank -- on the last audit date page 32."

You see that?

A. Yes, I do.

Q. You were referring to including a

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reference to the value of the intangible on page 32 of the PPM. Correct?

A. Correct.

Q. But this time you left the dollar figure blank. Right?

A. Correct.

Q. You didn't write 10 million. Correct?

A. No.

Q. And that is because you weren't sure what this was worth anymore. Right?

A. Correct.

Q. And you didn't get a response to point 4 of your e-mail, did you?

A. I don't remember getting a response.

Q. You don't recall ever getting a response. Correct?

A. Correct.

Q. And you never spoke with anyone at Waste2Energy about it. Correct?

A. No. Therein lies the problem. Yes. Correct.

Q. You don't recall having a conversation?

A. No.

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Q. In fact, you don't recall ever having a conversation with anyone at Waste2Energy about the $10 million asset. Correct?

A. Ever? Can you repeat the question, sir?

Q. I will withdraw it.

Now, Waste2Energy did not, in fact, include any reference to the $10 million number in the private placement memorandum, did it?

A. I don't recall.

Q. In fact, Waste2Energy didn't give any dollar value for its IP asset in the final private placement memorandum, did it?

A. That is correct I believe.

Q. That's correct; right?

A. I believe that is correct.

MR. JANGHORBANI: Mr. Chan, can you pull up Division Exhibit 3?

Q. Now, we have talked about this. This is the debenture private placement memorandum. And you reviewed this PPM when the final version came out; right?

A. Yes. I guess depending on how you define "review." I mean -- okay. Yeah, I

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reviewed it.

Q. Yes?

A. Yes.

Q. Now –

MR. JANGHORBANI: Mr. Chan, can I ask you to turn to page 31?

Q. Now, you see there is a section here on page 31 of the PPM entitled "Intellectual property"?

A. Yes, I do.

Q. You see that?

A. Yes.

Q. And you looked at this section. Correct?

A. Yes.

Q. And it is fair to say, isn't it, that there is no number given for the value of the IP asset here. Isn't that correct?

A. That is correct.

Q. And, in fact, this was the section you were asking, in your September 1st e-mail, you were asking Charles Vista to include the 10 million number in this section. Correct?

A. Well, based on the fact that it was

[p.224]

really there, yeah.

Q. Yes, you were asking them to include it in this section, page 31, intellectual property. Correct?

A. If they can legally put it in, yes.

Q. My question is only, was this the section -- you see this is page 31?

A. Well, I didn't specify what section. Maybe financial -- you know, we are going back a while.

MR. JANGHORBANI: I will withdraw my question.

Q. Now, just a few week after this, after September 9th, Waste2Energy's audited financials came out; correct?

A. Yes.

Q. They came out in two public files; right?

A. Right.

Q. A 10-Q. Correct?

A. Correct.

Q. And an amended Form 8-K. Correct?

A. Correct.

Q. And you received both those filings

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from your secretary. Correct?

A. I believe I did.

Q. And those financial statements showed that Waste2Energy had completely written off the $10 million asset. Correct?

A. Yes.

MR. JANGHORBANI: Mr. Chan, can you pull up Exhibit 16? This is already in evidence, your Honor.

Q. Do you see, Mr. Lorenzo, this is an amended Form 8-K of Waste2Energy?

A. Yes, I do.

Q. And if you turn to page 66, do you see it is signed by Craig Brown on October 1, 2009. Correct?

A. Yes.

Q. Mr. Brown, you understood, was the CFO at the time?

A. Yes, correct.

Q. This is the Form 8-K, the amended Form 8-K that you were just talking about?

A. Yes.

Q. That was sent to you by your secretary?

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A. Yes.

Q. Now, if you could turn to page 69, please? You see it says "Waste2Energy Inc. and subsidiaries consolidated balance sheet"?

A. Yes.

Q. You see there is a column that says "March 31, 2009"?

A. Correct.

Q. And you see there is a line that says "Total assets." Correct?

A. Correct.

Q. Next to that it says $370,552?

A. Correct.

Q. And that number was audited. Correct?

A. Correct.

Q. So it is fair to say that as of March 31, 2009, Waste2Energy's audited financial statements showed assets of under $400,000.

A. That is correct.

Q. You see the line for intangible assets gone; right?

A. That is gone, yes.

Q. You also see there is no line for goodwill?

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A. That is gone, too.

Q. If I could ask you to turn to page 46? You see there is a heading here that says "Asset impairment and bankruptcy of Enerwaste Europe subsidiary"?

A. Yes.

Q. You see that, sir?

A. Yes.

MR. JANGHORBANI: Mr. Chan, if you can highlight the last sentence of the paragraph starting, "As a result"?

Q. You see it says "As a result, an impairment charge in the amount of 10,538,029 was required to write off the value of the technology?"

You see that, sir?

A. Yes, I do.

Q. So it is fair to say Waste2Energy wrote off the $10 million asset?

A. Yes.

Q. And it was announcing it in this amended 8-K?

A. For the first time, yes.

Q. If you look at the last sentence of

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the next paragraph you see it says, "As a result of the above, management determined that goodwill was impaired and an impairment charge in the amount of $496,594 was recorded to write off the value of the goodwill."

Do you see that?

A. Yes, I do.

Q. So it is fair to say the company was also writing off about $500,000 in goodwill. Correct?

A. That is correct.

Q. If you add the two numbers together they are just about 11 million?

A. Give or take, yes.

Q. And I think you already said that your secretary e-mailed you this amended 8-K on October 1st. Right?

A. Yes, that is correct.

MR. JANGHORBANI: Can you, Mr. Chan, pull up Division 32?

Q. Do you have that in front of you, Mr. Lorenzo?

A. Yes.

Q. At the top it says from Sera Holmes to

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Francis Lorenzo and the date is October 1, 2009 at 4:55 p.m.?

A. Correct.

Q. So you received this e-mail. Correct?

A. Yes, I did.

Q. Sera Holmes was your assistant at the time?

A. She was the firm's assistant but I paid her. She worked for Charles Vista but I paid her.

Q. She had been with you since you were at Mercer. Correct?

A. Correct.

Q. She was your executive assistant. Correct?

A. Not at Charles Vista, though.

MR. JANGHORBANI: Your Honor, I would like to read another admission from the July 26, 2012 transcript, this time at page 24.

THE WITNESS: What date was that?

MR. JANGHORBANI: The July 26, 2012 testimony.

Page 24, your Honor, starting at line 5.

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May I read, your Honor?

JUDGE FOELAK: Yes.

MR. JANGHORBANI: "Question: Who is Sera Holmes?

"Answer: Sera Holmes has been with me since Mercer. She is my executive assistant."

Q. Did I read that correctly, Mr. Lorenzo?

A. Yes, you did.

Q. You can set that binder aside, sir.

I will move the admission of Division Exhibit 32.

JUDGE FOELAK: Exhibit 32 is admitted.

(So received in evidence as Division Exhibit 32.)

Q. You see there is a subject line here, sir?

A. Yes.

Q. It says "FW alert for Waste2Energy Holdings Inc." Then in block parentheses, "WTEZE." Then it says "Form 8-K/A."

You see that?

A. Yes, I do.

Q. Ms. Holmes is forwarding you a link to

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the amended 8-K?

A. Yes.

Q. That is the amended 8-K we just looked at; right?

A. Correct.

Q. That is Division 16. Correct?

A. Yes.

Q. You read that 8-K on October 1st, didn't you?

A. Probably not as closely as I should have, but yes.

Q. You did read it on October 1st. Correct?

A. Yes.

Q. In fact, you felt you had an obligation, didn't you, as the director of investment banking to review the amended 8-K?

A. Well, I reviewed the documents but I was -- for a material change nothing was brought to my attention prior --

Q. That is not my question, sir. You reviewed the 8-K because you felt you had an obligation –

A. That's correct.

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Q. – in your role as director of investment banking to review the Form 8-K. Correct?

A. Yes, that's correct.

Q. Earlier you testified that part of your job was to look at Waste2Energy's balance sheet. Correct?

A. Correct.

Q. So the write-down is announced right here on the balance sheet of this 8-K. Correct?

A. That's correct.

Q. And you read this 8-K, you just testified to that. Is that correct?

A. That is correct.

Q. So you knew on October 1st that the assets of the company were less than $400,000. Isn't that true?

A. I missed it.

Q. Isn't it the case that – withdrawn.

The reason you felt you had an obligation to review the 8-K was because an 8-K filed with the SEC is a material document. Isn't that true?

A. Yes, it is.

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Q. And in fact, it was so material that you forwarded this 8-K to all of Charles Vista's brokers. Didn't you?

A. Yes, I did.

Q. You did that almost immediately after getting it from Sera Holmes. Correct?

A. Probably, yes.

MR. JANGHORBANI: Mr. Chan, if I can ask you to turn to page 3?

Q. Now, you see there is an e-mail from you, correct, at 4:59 p.m., October 1st, to all brokers. Correct?

A. Correct.

Q. And it says "Subject, Waste2Energy Holdings files 8-K/A." Correct?

A. Correct.

Q. So you are forwarding the October 1st amended 8-K to all of the brokers at Charles Vista; right?

A. Yes.

Q. And you are sending it just four minutes after Sera Holmes sent it to you. Correct?

A. Correct.

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Q. And that is because this was an incredibly important document?

A. Well, it wasn't too important for them to tell me beforehand.

Q. But you thought it was an important document?

A. Yes, I thought it was important. Yes.

Q. Now, on October 1, 2009, Waste2Energy also issued a 10-Q you say. Correct?

A. I don't know if it was October 1st but it was close.

Q. It was around October 1st?

A. Give or take, yes.

Q. Why don't we just take a look at it.

Can you pull up Division 22? This is already in evidence, your Honor?

Q. Do you have the cover page of the 10-Q in front of you, sir?

A. Absolutely.

Q. You see it says, "Form 10-Q for quarterly period ended June 30, 2009" and the name of the company, Waste2Energy Holdings Inc. You see that?

A. Right.

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Q. It is fair to say this is a 10-Q of Waste2Energy. Correct?

A. Yes.

MR. JANGHORBANI: If I can ask you, Mr. Chan, to turn to the last page, page 45?

Q. Do you see it is signed by Peter Bohan and Craig Brown?

A. Correct.

Q. And Mr. Bohan was the chief executive officer of Waste2Energy?

A. Yes.

Q. And it was dated October 1, 2009. Correct?

A. Correct.

Q. So it is fair to say that Waste2Energy issued this 10-Q on October 1st. Correct?

A. Correct.

Q. Same day they issued the amended 8-K?

A. Correct.

MR. JANGHORBANI: Page 4, Mr. Chan?

Q. You see there is a condensed consolidated balance sheet for June 30, 2009 and March 31, 2009. You see that?

A. Correct.

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Q. You see the March 31st column?

A. Yes.

Q. Those were the same audited numbers we just looked at in the amended 8-K. Correct?

A. Correct.

Q. Is that a yes?

A. Yes.

Q. You see again total assets of under $400,000. Right?

A. Correct.

Q. Then you also see there is a column for June 30, 2009, "Unaudited." Do you see that?

A. Yes.

Q. Those numbers are not audited. Correct?

A. Correct.

Q. And you see total assets there are $660,408?

A. Correct.

Q. But there is still no line for intangibles. Right?

A. That is correct.

Q. And there is still no line for

[p.237]

goodwill. Right?

A. Correct.

Q. Now, this document, this Form 10-Q and the amended 8-K we just looked at, those were filed on October 1, 2009 and the numbers here are as of March

2009 and June 2009. But you didn't have any reason to think, did you, that these asset numbers had changed significantly between March and October 2009, did you?

A. I am sorry.

Q. Let me withdraw that. That was badly worded. This 10-Q is speaking as of June 30, 2009. Correct?

A. Yes.

Q. But it was filed on October 1, 2009. Correct?

A. Correct.

Q. You didn't have any reason to think, did you, that the numbers -- the numbers given here had changed significantly between June 2009 and October 1st. Correct?

A. Prior to October 1st?

Q. As of October 1st.

[p.238]

A. I am sorry. I am a little confused on the question. Can you give it one more try?

Q. Well, let me take another run at this. These numbers are here, the assets we are looking at, the balance sheet, the first column, those numbers are as of June; right?

A. As of June released October 1st.

Q. Right. But as of June. Correct?

A. Yes.

Q. The company -- you understood the company was saying, hey, we have about $660,000 in total assets on June 30, 2009. Correct?

A. But I became aware of that October 1st.

Q. That is not what I am asking you. You didn't have any reason to believe, did you, that this number, this total asset number had changed significantly on October 1st from what is listed here, did you?

A. Prior to October 1st I thought they had $10 million in assets.

MR. JANGHORBANI: Your Honor, I would like to read another admission. This is from the July 26, 2012 testimony. Page 120, your

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Honor.

THE WITNESS: What page?

MR. JANGHORBANI: Page 120, starting at line 19, your Honor. May I read, your Honor?

JUDGE FOELAK: Okay. It looks like he's there.

MR. JANGHORBANI: "Question: That is not what I am asking you. Let's start again. You see, but as we are looking at this it says as of March 31, 2009 the total assets are $370,552. Do you see that?

"Answer: Yes.

"Question: But this was issued on October 1, 2009. Are you following me?

"Answer: Yes.

"Question: On October 1, 2009, did you have any reason to believe that the assets as of October 1, 2009 were significantly different from the $370,000 figure that is here?

"Answer: I would not, no. I wouldn't be led to believe that it would have been different."

Q. Did I read that correctly, Mr. Lorenzo?

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A. I apologize but while you were reading I thought you said 118 so I was trying to catch up. It is 119. Correct? I am sorry.

Q. It is 120, sir.

A. What line?

Q. 19. Are you with me? It starts with "That is not what I am asking you."

MR. JANGHORBANI: May I read it again, your Honor?

JUDGE FOELAK: Certainly.

MR. JANGHORBANI: "Question: That is not what I am asking you. Let's start again. You see that as we are looking at this it says as of March 31, 2009, the total assets of $370,552. Do you see that?

"Answer: Yes.

"Question: But this was issued on October 1, 2009. Are you following me?

"Answer: Yes.

"Question: On October 1, 2009, did you have any reason to believe that the assets as of October 1, 2009 were significantly different from the $370,000 figure that is here?

"Answer: I would not, no. I wouldn't

[p.241]

be led to believe that it would have been different."

Q. Did I read that correctly?

A. Yes, you did.

Q. Thank you. You can set that binder aside, sir.

Now, you received this 10-Q, Exhibit 22, you received this on October 1st. Right?

A. Correct.

Q. And you read it; right?

A. Yeah, I am sure I did.

Q. And that's because once again you felt that in your role as director of investment banking you had an obligation to review your client's 10-Q. Correct?

A. That is correct.

Q. In fact, once again you sent this 10-Q to all of Charles Vista's brokers; right?

A. Yes, I did.

Q. And that is because it was an important document; correct?

A. That is correct.

Q. It was material. Correct?

[p.242]

A. Correct.

MR. JANGHORBANI: Mr. Chan, can you go to Division 21, please.

Q. Do you have that on your screen, Mr. Lorenzo?

A. Yes, I do.

Q. Mr. Lorenzo, if you could just let me finish my question? I have trouble with it as well but just to make the Court reporter's life easier?

A. No worries.

Q. You see this is an e-mail from you to all brokers. Correct?

A. Correct.

Q. It says, "Subject Waste2Energy Holdings Inc. SEC filings, Form 10-Q and Form 8-K/A." You see that?

A. That is correct.

Q. So you sent this e-mail. Correct?

A. That is correct.

MR. JANGHORBANI: I move the admission of Division 21, your Honor.

JUDGE FOELAK: Exhibit 21 an admitted.

(So received in evidence

[p.243]

as Division Exhibit 21.)

Q. You wrote "The following links are the recent W2E filings with the SEC." Correct?

A. Correct.

Q. That meant Waste2Energy. Correct?

A. Correct.

Q. Then there is two links. Right?

A. Yes.

Q. One is for a Form 10-Q, correct, and one is for a form amended 8-K. Correct?

A. That is correct.

Q. So you are forwarding links to the two filings we just looked at to all Charles Vista's brokers. Correct?

A. That is right.

Q. Now, these filings -- we just looked at them. These are the ones that disclose that waste to energy had written off all its intangible assets. Right?

A. Correct.

Q. And its goodwill. Correct?

A. Correct.

Q. By far the lion's share of its assets. Correct?

[p.244]

A. That is correct.

Q. That announcement was a big deal to you; right?

A. I am surprised I didn't hear about it sooner. Yes, it is a big deal.

Q. It was a big kick in the stomach, wasn't it?

A. Yeah.

Q. Is that a yes?

A. Yes.

Q. And that is because it counted for almost all of Waste2Energy's assets on its balance sheet. Right?

A. Correct.

Q. Now, these filings, these weren't the last time you were told about the write-off, were they?

A. The last time I was told? These weren't the last time I was told?

Q. These October 1st filings, these were not the last time you were told about the write-off; isn't that fair to say?

A. I think that is accurate to say.

Q. In fact, Craig Brown told you again

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about the write-off just five days after this filings came out; right?

A. I received an e-mail from Craig Brown forwarded from Andre. But as far as discussing the implications of this asset, no.

Q. So you received an e-mail from Craig Brown telling you about the write-off on October 5th. Correct?

A. Yeah, the one from Andre. Right?

Q. I am just asking –

A. If I am thinking it is the right – if I am thinking of the right one, yes.

Q. And you read that e-mail. Correct?

A. I don't remember reading it. I mean I may have read it. Probably skimmed it.

MR. JANGHORBANI: Mr. Chan, can you pull up Division 19?

Q. This is an e-mail from Craig Brown to a number of people, including yourself. Correct?

A. Correct.

Q. It is dated October 5, 2009. Correct?

A. Correct.

Q. The subject is "Re: W2E financial

[p.246]

filings." Correct?

A. Correct.

Q. You read this e-mail at the time you received it. Correct?

A. You know, I don't know what I testified to. I may have skimmed it but, you know – I may – I probably

skimmed it but there was no -- there was no follow-up, there was nothing significant about this e-mail at the time.

Q. There was nothing significant about this e-mail?

A. It was --

Q. That is not the question I asked --

MR. HANTMAN: Let him finish.

JUDGE FOELAK: Let him finish.

A. I was counting based on the agreements with Waste2Energy that any significant development would be voluntarily disclosed and not put into an e-mail.

Q. Right, right.

MR. HANTMAN: Your Honor, I object to the snide remarks, "Right, right." Counsel may not like the answer but doesn't need to be

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demeaning to the witness.

JUDGE FOELAK: The "right, right," is withdrawn.

A. With all due respect, the company's debentures -- Waste2Energy began working on this write-down in July.

MR. JANGHORBANI: Your Honor, we are far afield of the question I asked. All I asked is whether he received and read the e-mail. I have a right to an answer to my question.

THE WITNESS: This was an unintentional miss. There wasn't a preconceived, premeditated -- this was a miss because these events were not brought to my attention. And something this significant shouldn't have been just put into an e-mail and hid into a filing.

There needs to be a meeting about this, have a contingency plan. The default provisions needed to be changed, the PPM's needed to be amended. There needed to be a plan if this asset was -- was reduced, not just thrown into an e-mail in the last minute.

The company signed an investment

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banking agreement saying that they would voluntarily disclose material financial information when they received and became aware of that information.

They became aware of this in July. I am only hearing about it now. And then I --

MR. JANGHORBANI: Your Honor --

MR. HANTMAN: Let him finish before the objection.

MR. JANGHORBANI: Mr. Lorenzo will have an opportunity to testify, will have an opportunity to have a direct examination. I asked a very straightforward question and I think I'm entitled to a response.

JUDGE FOELAK: The idea is he is asking you a question that you may wish to expound upon but your attorney will bring out everything you want to say.

THE WITNESS: I apologize to the Court. I am sorry, sir.

JUDGE FOELAK: No problem.

MR. JANGHORBANI: Let me start again.

Q. It is obvious you got this e-mail. Correct?

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A. Yes.

Q. And you reviewed it; correct?

A. Reviewed it, yes.

Q. And you remember reviewing it. Correct?

A. If I remembered reviewing this I would have never sent out those two other e-mails, period. I don't care what you say.

MR. JANGHORBANI: Your Honor, I would like to read another admission from the July 2012 transcript.

MR. HANTMAN: Your Honor --

MR. JANGHORBANI: May I finish, please? This time it is page 138, line 5, starting line 5.

THE WITNESS: What was the date, sir?

MR. JANGHORBANI: The July 26, 2012 transcript, page 138, beginning at line 5.

JUDGE FOELAK: Wait. Mr. Hantman?

MR. HANTMAN: I want to inject so the record is clear, these transcripts, this is the fourth transcript or hearing of this witness and this is the first time that he is being deposed or he is at this hearing without the opportunity

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to have counsel with him.

MR. KAUFMAN: He had the opportunity –

MR. HANTMAN: Your Honor, he didn't have counsel there. Three other times they tried to get all this information they couldn't do it. The time he doesn't have counsel with him, then they harp on all these different things. I just want to put it in the right perspective.

JUDGE FOELAK: Context. Okay.

MR. HANTMAN: It doesn't call for any comment. This is the fact of the case.

MR. JANGHORBANI: This is argument and Mr. Hantman will have opportunity to make argument.

JUDGE FOELAK: Fine. Let's move forward.

MR. JANGHORBANI: May I read, your Honor?

MR. HANTMAN: Well, I am not satisfied with that because it is not argument. It is undisputed –

JUDGE FOELAK: No, no. Are you at the

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place where he wants to start reading?

MR. HANTMAN: Sorry, your Honor.

THE WITNESS: What line?

MR. JANGHORBANI: Page 138, starting line 5.

THE WITNESS: I am ready.

JUDGE FOELAK: Go ahead.

MR. JANGHORBANI: "Question: Do you remember seeing this information, getting this e-mail and learning about this on October 5, 2009?

"Answer: It's obvious I got the e-mail. I remember reviewing it. Okay. Yes. I do remember reviewing this."

Q. Did I read that accurately?

A. Yes, you did.

Q. Thank you.

Now, Mr. Brown tells you right here on page 1 about the write-off. Correct?

A. Yes.

Q. And that is point 2. You see that?

A. Yes, I do.

Q. And he writes, "Write-off of all of our intangible assets that were tied to our

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purchase of Enerwaste in March 31st period of about $11 million." You see that?

A. Yep.

Q. So you understand Mr. Brown is referring to the same intangible assets we have been talking about. Right?

A. Correct.

Q. You understood that at the time. Correct?

A. At the time of what?

MR. JANGHORBANI: Withdrawn.

Q. So it is fair to say, isn't it, sir, that on October 5, 2005, you were aware that the $10 million asset had been written off by Waste2Energy. Correct?

A. Okay. I will agree to that. That's correct.

Q. That is a fair statement?

A. Yes.

Q. And it is also fair to say, isn't it, sir, that nobody ever gave you any inaccurate information about the $10 million intellectual property asset?

A. That is not fair. That is not an

[p.253]

accurate statement.

Q. You can't remember anyone giving any inaccurate information, can you?

A. That – is omitting material financial statements, is that inaccurate information?

Q. I will try the question again, sir.

You can't remember anyone ever giving you any inaccurate information about the $10 million asset. Isn't that correct?

A. That is not correct.

MR. JANGHORBANI: Your Honor, I would like to read another admission from the same transcript, the July 26, 2012 transcript, starting from line 6, your Honor.

JUDGE FOELAK: Of what page?

MR. JANGHORBANI: Page 53, line...

May I read, your Honor.

JUDGE FOELAK: Go ahead.

MR. JANGHORBANI: "Question: As you sit here today, you don't remember anybody gave you inaccurate information about the $10 million intellectual property asset?

"Answer: I can't remember, no."

Q. Did I read that correctly, sir?

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A. Yes, you read it correctly.

Q. Now, Mr. Brown wrote to you on October 5th, just a couple weeks after this e-mail --

You sent an e-mail to two prospective investors saying the $10 million asset still existed. Isn't that correct?

A. That's correct.

JUDGE FOELAK: We'll take 15 minutes.

(Recess.)

JUDGE FOELAK: Out of curiosity, how much longer do you expect with the witness?

MR. JANGHORBANI: It all depends on the answers I get, but in my outline I am over halfway through.

JUDGE FOELAK: Perhaps Mr. Hantman will defer his examination until tomorrow.

MR. HANTMAN: I am pretty sure.

MR. JANGHORBANI: I would love to get through it all today, your Honor.

JUDGE FOELAK: But there is no point in going overboard.

MR. HANTMAN: If counsel wants to put in the date and the page and line number we'll

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stipulate that that can be introduced into the record. We'll have an opportunity to put in at some point whatever pages or lines we want so we can avoid all this testimony.

MR. JANGHORBANI: No, your Honor. We can't stipulate to that for a couple of reasons. One, this is part of our presentation. I think it is important to put in statements that directly contradict what the witness is saying now.

But, two, these are offered as admissions against a party opponent. Mr. Hantman cannot offer admissions of statements of his own client of his own prior testimony because they are not offered against a party opponent.

JUDGE FOELAK: Sometimes the parties mutually agree on -- well, okay.

MR. HANTMAN: I know counsel likes the dramatic of confronting the witness with the statements. I can appreciate that. I am suggesting there may be other parts of the testimony which would elaborate on --

JUDGE FOELAK: Counter-designate.

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Yes.

MR. HANTMAN: Or give some realistic context to the points being made. This is more like argument.

MR. JANGHORBANI: First of all, it is not argument.

JUDGE FOELAK: Okay, okay. But --

MR. JANGHORBANI: Be that as it may, maybe counsel can talk about this after the Court closes today.

JUDGE FOELAK: Would you have in mind 5 or 5:30?

MR. JANGHORBANI: I will take direction from your Honor.

JUDGE FOELAK: Well, why don't we start now.

MR. JANGHORBANI: Your Honor, can I have the last question and answer read back just to reorient us?

(Record read as follows: "Now, Mr. Brown wrote to you on October 5th, just a couple weeks after this e-mail -- you sent an e-mail to two prospective investors saying the $10 million asset still existed.

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Isn't that correct?

"Answer: That's correct.")

CONTINUED DIRECT EXAMINATION

BY MR. JANGHORBANI:

Q. And in fact, you told them the $10 million was one of the things that protected their investment in Waste2Energy debentures. Correct?

A. I told them?

Q. In your e-mail. Correct?

A. I cut and paste an e-mail and sent it to them. Yeah.

MR. JANGHORBANI: Mr. Chan, can you open Division 34? This is in evidence, your Honor.

Q. You have that on your screen, sir?

A. Yes.

Q. You see this is an e-mail from you to W.S. Rothe at Sbcglobal.net?

A. Correct.

Q. You sent this on October 14, 2009. Correct?

A. Yes.

Q. W.S. Rothe is William Rothe. Correct?

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A. Yes.

Q. You see that is your signature block on the bottom. Correct?

A. Yes.

Q. It says "Truly, Francis V. Lorenzo, vice president investment banking." Correct?

A. Yes.

Q. You see if you turn to the first page of the e-mail -- I did this out of order.

There is another e-mail from you to Vishal Goolcharan also October 14, 2009. Correct?

A. Correct.

Q. You also sent that e-mail. Correct?

A. Correct.

Q. And you also have your signature block on that. Correct?

A. Yes, I do.

Q. Now, you write in the subject line "W2E debenture deal points." You see that?

A. Yes, I do.

Q. So we are talking about the $15 million debenture offering, correct --

A. Correct.

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Q. -- that was going on at the time. Right?

A. Correct.

Q. And we have looked at the private placement memoranda for that document earlier today. You recall that?

A. Yes, I do.

Q. I just turn you back to that -- before I do that, the debentures were highly speculative. Right?

A. Yes, they were.

Q. They involved a high degree of risk. Correct?

A. Correct.

Q. And this e-mail -- these two e-mails here, Exhibit 34, these e-mails contain material information about the debenture offering. Correct?

A. Correct.

Q. In fact, when you wrote "W2E debenture deal points --" well, withdrawn.

Now, you sent this e-mail, didn't you, to summarize several key points of the Waste2Energy Holdings debenture offering.

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Right.

A. Mistakenly so, that is correct.

Q. You weren't summarizing key points, sir?

A. Well, I made a mistake. Yes. I sent out inaccurate information in an e-mail.

Q. Right.

A. Correct.

Q. Mr. Goolcharan, he invested $15,000, right, in debentures?

A. I found that out through you guys.

Q. You heard Mr. Brown testify to that earlier?

A. That's correct.

Q. You didn't discuss either of these deal point e-mails with Gregg Lorenzo, did you?

A. I didn't discuss either of these deal point e-mails? You mean the actual e-mail?

Q. You didn't discuss the deal point e-mails with Gregg Lorenzo, did you?

A. No. I got the e-mail addresses from him. Of course I discussed it with him.

Q. Well, you didn't discuss the subject matter of either of these e-mails with

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Mr. Mr. Lorenzo, did you?

A. Me, Mike and Gregg -- this was authored by me, Mike and Gregg.

Q. So you, Mr. Lorenzo and I assume you mean Mr. Molinaro, you guys authored this e-mail?

A. If memory serves me -- I think I authored it and then it was approved by Gregg and Mike.

Q. All right.

A. But you are going back aways and it was confusing.

Q. So you authored it and you believe that it was approved by Gregg Lorenzo and Mike Molinaro. Is that your testimony?

A. I don't really recall --

Q. Withdrawn.

A. -- exactly.

Q. But you didn't discuss the subject matter of these e-mails with Gregg Lorenzo, did you?

A. I was asked to send these e-mails out by Gregg Lorenzo to two of his clients and unfortunately I did.

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MR. JANGHORBANI: Your Honor, I would like to read another admission from the July 26, 2012 transcript, page 144.

THE WITNESS: 144?

MR. JANGHORBANI: 144, starting line 1.

May I read, your Honor?

JUDGE FOELAK: Are you there?

MR. HANTMAN: Sorry. What page?

MR. JANGHORBANI: 144.

MR. JANGHORBANI: Line 1.

"Question: Just going back to the October 14, 2009, e-mails that you sent, Exhibit 115, did you discuss either of the e-mails or the subject matter of the e-mails at all with Gregg Lorenzo?

"Answer: Not that I recall.

"Question: Do you have any reason to believe that you did discuss it?

"Answer: No. If this is the guy I think it is, they kept me away from that whole thing."

Did I read that correctly, sir?

A. Yeah.

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Q. Now, this e-mail, Division 34 – it is really two e-mails but we are looking at the body of the first one now. You see about midway down it says there are three layers of protection?

A. Correct.

Q. Okay. You see the first one says the company has over 10 million in confirmed assets?

A. Correct.

Q. You are referring to the intangible asset we talked about earlier?

A. Yes.

Q. So you are saying that investors were protected from loss because Waste2Energy had millions in intangible assets. Correct?

A. That is what I said, yes.

Q. Millions in assets. Correct?

A. Correct.

Q. Now, your statement that Waste2Energy had over 10 million in confirmed assets, that wasn't accurate on October 14th, was it?

A. Nope. No, it wasn't.

Q. You knew that statement was inaccurate when you sent this e-mail, didn't you?

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A. No. I can't say that a hundred percent.

Q. Well, you knew it was misleading at the time, didn't you?

A. You know, I am sure future -- when Robert -- I just made a mistake and sent it. I cut and pasted and sent it. I made a mistake.

Q. Well, that is not true, is it? Didn't you know this e-mail was misleading at the time that you sent it?

A. I am going to stick by the fact that I made a mistake.

Q. All right.

A. I didn't consciously intend to -- to mislead anybody. I just -- I have never done it before and I just don't know why I would do it now.

Q. Sir, you can't sit here now, can you, and say that you did not know that this e-mail was false when you sent it, can you?

A. I can't say I consciously sent out an e-mail with bad information with the intent to mislead anybody. I can't say I consciously did that. I may have made a mistake and wasn't

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thinking, but consciously try to send bad information to somebody? I cannot sit here and say that I did that under oath with the intent --

MR. JANGHORBANI: Your Honor --

THE WITNESS: -- with the intent of myths leading somebody. I cannot say that.

MR. JANGHORBANI: Your Honor, I would like to read another admission from the July 26, 2012 transcript. It starts on page 140, if Mr. Hantman is with us.

MR. HANTMAN: I am with you.

MR. JANGHORBANI: 140.

THE WITNESS: Line?

MR. JANGHORBANI: Starts line 24 and goes over on to the next page.

May I read, your Honor?

JUDGE FOELAK: Yes.

MR. JANGHORBANI: "Question: And this e-mail, in the body of it, it has three layers of protection. Do you see that?

"Answer: Yes, I do.

"Question: You have already testified that at least the first two -- I think actually

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you testified the first two are inaccurate and the third can be interpreted as misleading. Is that correct?

"Answer: It depends on how you interpret it, the third. Okay.

"Question: My question is, did you know that those statements were inaccurate and misleading?

"Answer: Yes.

"Question: You knew at the time?

"Answer: At the time? I can't sit here and say that I didn't know."

Q. Did I read that correctly, Mr. Lorenzo?

A. Yes, you did.

Q. And that was because -- withdrawn.

You see you also say this first layer, this first purported layer of protection, you say the $10 million assets are confirmed. Right?

A. Yes.

Q. That was never true, was it?

A. No.

Q. That is because you took this number

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from an unaudited 8-K. Correct?

A. Yes, I believe that is correct.

Q. That number had never been confirmed by any auditor. Correct?

A. Correct.

Q. In fact we looked at documents earlier today, didn't we, showing that you asked Waste2Energy in August and September to confirm that number, didn't you?

A. Yes, I did.

Q. The company never confirmed it, did it?

A. No.

Q. Even before you received the audited financials you understood, didn't you, that the $10 million asset did not provide any protection to debenture holders. Isn't that right?

A. Sorry. What was that? Can you say that again?

MR. JANGHORBANI: Your Honor, may I have the question read back?

(Record read.)

A. Any protection?

Q. Yes.

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A. Any? Like zero protection?

Q. You understood it didn't provide any protection to a debenture investor, didn't you?

A. Not $10 million of protection, but there was something there.

Q. Well, you testified earlier you thought it was a dead asset. You remember testifying that way?

A. I believe I said you would get 10 percent of the value if you are lucky.

Q. I think you actually testified that the company would be lucky to get a million dollars for it? Isn't that true?

A. That's correct.

Q. Isn't it also true you told Gregg Lorenzo in August 2009 that Waste2Energy would be lucky to get a million dollars for those assets?

A. Sounds like something I would say to him, yes.

Q. You said that?

A. Yes.

Q. In fact you told Gregg Lorenzo all the time from March or April 2009 all the way up to

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October 2009 not to sell the debentures as being collateralized with this asset. Correct?

A. Makes it seem like this is a mistake, don't it?

Yes.

Q. And that is because you knew that this $10 million asset provided no protection. Correct?

A. That is correct.

Q. And you understood, didn't you, that if there was a default on a debenture, clients would not be able to recoup their money based on a liquidation of this asset. Correct?

A. Recoup all of their money? Any of their money?

I would say your statement is accurate.

Q. Now, the second layer of protection that you talk about here, you wrote that the company has purchase orders and LOI's for over 43 million in orders. You see that?

A. Correct.

Q. So in other words you are saying that investors were protected from loss because

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Waste2Energy had millions in purchase orders and letters of intent. Correct?

A. Protected from loss? I mean, the debentures were not formally – there were no UCC's or collateralization formally against these debentures.

Q. So you weren't saying here that the company's purchase orders and LOI's for over $43 million was a layer of protection?

A. It may be a layer of protection.

Q. Well, those are in fact the exact words you used; correct?

A. Yeah, okay. Makes sense.

Q. That was misleading, wasn't it?

A. I would say that is misleading -- well, according to Peter Bohan it wasn't misleading. But for what you are getting at, I could see it being misleading.

Peter Bohan has always put a lot of confidence in the purchase orders and LOI's.

Q. Sir, I haven't asked you what Peter Bohan thought.

A. Okay.

Q. I am asking you what you knew. You

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knew this was misleading; isn't that true?

A. I knew that this was misleading? Perhaps – I can't say that with a hundred percent accuracy, that I knew one hundred percent that this was misleading. I mean, idealistic? Yes. Misleading? I can't say that with a hundred percent because they did have LOI's for 43 million.

Anyhow, I knew that this was misleading?

MR. JANGHORBANI: Your Honor, I would like to read another admission from page 141 of the July transcript.

THE WITNESS: What was the number?

MR. JANGHORBANI: Page 141, starting at line 14.

JUDGE FOELAK: Okay.

MR. JANGHORBANI: "Question: My question is, did you know that those statements were inaccurate and misleading?

"Answer: Yes.

"Question: You knew that at the time?

"Answer: At the time? I can't sit here and say that I didn't know."

[p.272]

Q. Did I read that accurately, sir?

A. Yes, you did.

MR. HANTMAN: Your Honor, this is a repetition of what was read previously.

MR. JANGHORBANI: There is more than three, but there are three different representations here. He admitted earlier all three are false, your Honor. Now on the stand he is trying to take some of that back.

JUDGE FOELAK: Well, he said "I can't say I didn't know." That isn't quite the same as saying I did know.

THE WITNESS: Thank you.

MR. HANTMAN: And he was asked the question like three times before he gave a different answer.

JUDGE FOELAK: Okay. Let's move on.

MR. JANGHORBANI: Just to correct the record, he says right before that -- my question is "Did you know those statements were inaccurate and misleading?" "Answer: Yes." But I will move on.

Q. Now, there were no purchase orders for 43 million in orders. Correct?

[p.273]

A. At the time, I thought there were purchase -- I mean, I just -- I just have a hard time remembering exactly all the -- what I testified to and juggling my memory now.

I know that Peter Bohan -- because I brought this up to Peter Bohan -- was adamant about the confidence of the LOI and the purchase orders. I know that.

Whether they were -- whether they came to fruition or not, probably not. But Peter Bohan put a lot of credence in these purchase orders and LOI's.

Q. Once again, I am not asking about what Mr. Bohan knew. I am simply asking you, there were no purchase orders for $43 million in orders on October 14th; isn't that true?

A. There was an LOI. Okay. Yes. Correct.

Q. And in fact all you had ever seen by October 14th were projections of future sales. Correct?

A. That is -- yes. That is accurate.

Q. In other words, sales that Waste2Energy hoped would materialize. Correct?

[p.274]

A. That is correct.

Q. And this 43 million that we see here in Exhibit 34, that refers to one non-binding letter of intent. Correct?

A. Yes. St. Martin. Yes, that is correct.

Q. And you doubted that the 43 million LOI would ever result in any sales. Isn't that correct?

A. After the Benkovsky money, yes. Before the Benkovsky money, no, depending on when you are asking.

MR. JANGHORBANI: Mr. Chan, can I ask you to pull up Division 29, please.

Q. Do you have that on your screen, Mr. Lorenzo?

A. Yes.

Q. This is an e-mail from you to Lloyd McAdams; correct?

A. That is correct.

Q. Copying Gregg Lorenzo and Michael Molinaro; right?

A. Correct.

Q. And says "Waste2Energy projections."

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Correct?

A. Yes.

Q. You sent this e-mail?

A. Yes.

Q. There is an attachment to the e-mail. You see in the attachment line "Waste2Energy projections 2009"?

A. Yes.

Q. You sent that attachment as well?

A. Yes, I did.

MR. JANGHORBANI: Your Honor, I move admission of Division 29.

JUDGE FOELAK: Exhibit 29 is admitted.

(So received in evidence as Division Exhibit 29.)

Q. Now, you see you write that you are attaching the Waste2Energy projections. Correct?

A. That is correct.

Q. And you mean projected sales of Waste2Energy's products. Right?

A. Projected sales. Yes.

Q. Not actual sales?

[p.276]

A. Not actual.

Q. Not confirmed purchase orders. Correct?

A. Well, I will let you know when I see it. I don't know if there were purchase orders on these

projections. Maybe just -- I don't know. I don't see the projections. It's been a while. I know that Peter Bohan put several different types of projection schedules together.

MR. JANGHORBANI: Mr. Chan, can you turn to the first page of the attachment? I think it is the third page of the document.

Q. This is the first page of the attachment, sir?

A. Yes.

Q. You see it says Caribbean Island, next to that, 43 million, next to that "LOI received?"

A. Yes.

Q. That is the $43 million letter of intent you are talking about in the deal points e-mail?

A. Yes, that is correct.

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Q. This refers to a potential sale in the island of St. Martin?

A. Yes. That is correct.

Q. That means that a customer was interested in purchasing Waste2Energy's units?

A. Correct.

Q. Didn't mean the customer actually had to purchase those units; right?

A. That is correct.

Q. And the St. Martin customer never came through with the purchase; right?

A. Not to my knowledge, no.

Q. And by September 2009 you didn't think it was ever going to come through; right?

A. That is after the Benkovsky money? That is correct.

Q. I am asking you for your best recollection. Isn't it true that by September 2009 you didn't think that the 43 million LOI was ever going to turn into purchases?

A. I didn't think anything was going to come through after the Benkovsky money was spent. I think Benkovsky was end of August, so

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your statement would be accurate.

He made his $2 million investment end of August and nothing significant happened with Waste2Energy after that so I lost confidence in all developments after -- I think what you said it accurate. In September, probably mid to late September.

Q. So sometime in September you lost confidence that this 43 million was ever going to happen?

A. Yes.

Q. Including this 43 million, there is no other number on this page that is not a projection. Right?

A. There is no other number on this page?

Q. That was a terrible question. Let me ask again. I apologize.

All the numbers on this page are projections. Correct?

A. This page here that I am looking at?

Q. Yes.

A. Caribbean? Dargavel? Yes. All projections.

Q. None of these numbers equated to

[p.279]

actual sales to your knowledge?

A. Maintenance contract. The three-year maintenance contract could have been tangible. It says contract.

Q. For $725,000?

A. Yes. It does say contract and I know that they did have some revenues from --

Q. Are you just speculating now?

A. I don't remember.

MR. JANGHORBANI: Your Honor, I would like to read another admission from the July 26, 2012 transcript. Page 74.

MR. HANTMAN: Your Honor, if I may, I would like to move the entire transcript into evidence because --

JUDGE FOELAK: I will tell you what, Mr. Hantman. The Commission has cast a disapproving eye

on moving entire transcripts, but perhaps you could, after the hearing is over, counter-designate selected portions.

MR. HANTMAN: Well, just to move this trial along, rather than do this piecemeal in the course of direct or redirect testimony, I would like to reserve the right in any

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post-trial submission to put in things just from the record.

MR. JANGHORBANI: Your Honor, may I be heard on that point?

JUDGE FOELAK: I didn't actually mean -- what I meant was within a reasonable time after the hearing close, to counter-designate selected portions.

MR. HANTMAN: That would be fine, once I get the transcript --

JUDGE FOELAK: Then they would become part of the record.

MR. JANGHORBANI: Once I get the transcript so I can see exactly what page and line and study it. Now it is virtually impossible, not knowing what page or line the government is going to rely upon to go into the record to find something maybe in a whole different section which would explain something away or at least mitigate it or provide the right context.

MR. JANGHORBANI: Your Honor, the rules are clear that the evidence that forms the file is the evidence that comes in at the

[p.281]

hearing. We would strenuously object to Mr. Hantman being able, after the hearing closes, to go back and reconsider whatever evidence he wants to put in.

JUDGE FOELAK: Okay. In that case, you can mutually agree on additional portions. I take his point, but in many cases, in order to avoid putting in the entire transcript the parties do mutually agree.

MR. HANTMAN: Why don't we try to work this out and if we can't reach a resolution then we can make the appropriate application to the Court.

JUDGE FOELAK: Okay. That sounds good.

MR. JANGHORBANI: May I? Page 74, beginning line 19. May I read, your Honor?

JUDGE FOELAK: Yes.

MR. JANGHORBANI: "Question: Is there any number on here that is not a projection as you understand it?

"Answer: In other words, is there any number on here that actually had been realized as gross revenue?

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"Question: Either that or the actual sale contract.

"Answer: No. I don't believe any of this equated into sales to my knowledge.

Q. Did I read that correctly, Mr. Lorenzo?

A. Yes, you did.

Q. This e-mail that you sent, Division Exhibit 29, you sent that on August 3, 2009. Right?

A. I guess so. I am looking at the schedule --

MR. JANGHORBANI: Mr. Chan?

A. Yes.

Q. That was over two months before October 14th. Right?

A. Yes.

Q. Now, going back to Exhibit 34, the deal points e-mail --

Your Honor, I move Exhibit 29 into evidence. I think I forgot to do that -- oh, co-counsel tells me we moved it already.

JUDGE FOELAK: Yes.

MR. JANGHORBANI: I apologize. Long

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day.

Q. Exhibit 34, you see here the final layer of protection you refer to, that number 3?

A. Yes.

Q. You say that "Charles Vista has agreed to raise additional money to repay these debenture holders if necessary"?

A. Correct.

Q. So, in other words, you are saying that if Waste2Energy cannot for some reason pay back the 12-percent debenture holders Charles Vista would raise additional money to pay them back. Correct?

A. That is Gregg Lorenzo saying "I will pay you back. I will pay you back." That is what that is.

Q. That wasn't accurate; right?

A. Well, Gregg believed it.

Q. I am asking you. It wasn't accurate, was it?

A. Well...

MR. HANTMAN: Objection to the form of the question whether it is accurate or not.

A. I don't know if it is accurate or not.

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The kid raised money to pay back previous debentures in the past. Maybe he could, maybe he couldn't.

But as far as a formal agreement with debenture holders in the note, the actual note, I don't think there was a reference that there would be additional money raised from Charles Vista in a default event to pay the note.

Q. There wasn't an actual agreement in the note?

A. There was no actual agreement. I think that is accurate.

Q. And there wasn't an actual agreement between Waste2Energy and Charles Vista to do that; right?

A. No. That was just Gregg Lorenzo saying: Yeah, I will take you out, I will raise more money." That is some --

Q. So you agree with me, wouldn't you, that you can interpret this last layer of protection as being misleading. Correct?

A. Yeah. I'd say -- you couldn't hang your hat on it. Put it that way.

Q. In order to raise money Charles Vista

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would have to find people to invest in Waste2Energy; right?

A. Find accredited investors, yes.

Q. It needs to find investors willing to invest; right?

A. Accredited investors. Yes.

Q. You didn't think at the time, you didn't think Charles Vista would be able to do that. Right?

A. To do -- at the time, what time?

Q. As of October 14, 2009, you didn't think that Charles Vista would be able to find investors willing to invest additional monies in Waste2Energy?

A. Additional monies, meaning existing shareholders putting more money in, or new shareholders putting new money in?

Q. Meaning you didn't think that Charles Vista would be able to raise additional money to repay debenture holders. Correct?

A. I'd say that that's accurate, yes.

Q. And that is because Waste2Energy was not a good investment. Right?

A. I am sure they would be able to raise

[p.286]

some money, but enough money to sustain growth, pay operations and repay debentures holders? I think that would be a stretch.

Q. You thought that at the time; right?

A. Yeah, yeah. After Benkovsky's 2 million, my point of view dramatically changed. Yes, that is accurate.

Q. And you didn't think that Waste2Energy debentures were a good investment. Correct?

A. That is not a hundred percent correct.

Q. That is not correct?

A. Not a hundred percent correct. There is more going on in that question than just the question.

I think that if it was positioned as a pure risk capital investment where, you know, you maybe put 2 percent of your investment, the overall portfolio into this type of situation and you knew it was high risk and you had the resources, perhaps you put up a dollar to make $5. But the investor would have to understand that fully and totally prior to the investment.

So, if it was a hundred percent bad, bad investment? I can't agree with that fully.

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I think if it was handled properly it still perhaps had some value.

Q. You didn't think that Waste2Energy would be able to raise enough money to meet its default obligations, did you?

A. Raise enough money to repay notes, you mean repay notes with investment capital? Solely and exclusive repay the note with investment capital?

Q. They wouldn't be able to raise enough money to keep from defaulting on its prior obligations. Correct?

A. Raise enough -- well, if they -- well, it was never the intention of repaying notes with new notes. The intention to repay the notes was with the proceeds from corporate growth. So although it turned out that the company didn't grow on the corporate side to repay the notes and meet default -- so it turned out that they were raising new money with new notes to pay old notes. But that was not the intention.

So, to answer your question, they wouldn't be able to raise new investment capital

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to pay defaulted notes. They wouldn't be able to raise new investment capital to pay defaulted notes. The notes were supposed to be repaid with gross revenue purchase orders and, you know, the operations of the company.

Q. You didn't think this debenture investment was a worthwhile investment; right?

A. At this stage?

Q. October 14th?

A. Yes, that's correct.

Q. And that is because Waste2Energy's financial condition was horrible. Right?

A. That's because prior -- I say this in my testimony. Forgive me if -- I don't remember everything I said in my testimony, so maybe I made a couple of unintentional mistakes.

But one thing I do know is that prior to Steven Benkovsky's $2 million, Waste2Energy always said they never got enough money to really grow the business. And that made sense. They only had enough money to repay angry noteholders and to pay operations.

But when they got Benkovsky's 2 million all at once and they still couldn't

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grow the company properly with that big tranche of money, that is when my point of view changed and I lost confidence in the management of Waste2Energy to grow the business.

Q. Okay.

A. So it is all really dependent on that 2 million, before and after.

Q. In fact, with this 12 percent debenture offer we have been looking at, Waste2Energy needed to sell $4

million of those debentures just to be able to pay back earlier debt. Correct?

A. That sounds accurate. And there were -- there were proposals made to Gregg Lorenzo in order to mitigate this risk but he didn't -- he didn't use them.

Q. All right. And you thought it was highly unlikely, didn't you, that Waste2Energy was going to have enough corporate growth in order to pay back the money that it had borrowed. Right?

A. Yeah. Kind of like in October, mid -- yeah. Kind of that whole September, October thing kind of changed everything around. Yes.

[p.290]

Yes, I'd say that's accurate.

Q. In fact you knew that Waste2Energy needed to grow by about 21 percent just to pay back the money it had borrowed. Right?

A. It needed to grow at 21 percent to repay the money it borrowed? I think I said that somewhere. That number rings a bell.

Q. That is accurate?

A. I think I even said that in my testimony.

Q. And that is accurate?

A. Yes. As memory serves me, yes.

Q. By comparison, a Dow Jones company grows 14 to 16 percent?

A. The multiple is. I don't know what the gross is but the multiple is.

Q. Waste2Energy wasn't a Dow Jones company; right?

A. No. That is accurate. I will agree with you on that one.

Q. So highly unlikely that it would be able to grow enough to pay debenture holders back. Right?

A. I'd say Peter Bohan would have

[p.291]

disagreed but I'd say that's accurate.

Q. Didn't you also know in October 2009 that if Waste2Energy defaulted on its 12-percent debentures it would be very difficult for it to raise additional money?

A. Absolutely, yes, I knew.

Q. It would severely compromise Waste2Energy's ability to raise more money. Right?

A. I knew that long before October, yes. Go ahead.

Q. Why would you lend money to a company that was unable to pay back its prior investors; right?

A. That is correct.

Q. Charles Vista had already -- sorry. Withdrawn.

Charles Vista, we have been talking about the investment banking operations. Charles Vista was also a registered broker-dealer?

A. Correct.

Q. And as of October 2009 Charles Vista had already put too many of its brokerage

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clients into Waste2Energy. Correct?

A. That is my opinion, yes.

Q. In fact, about 70 percent of Charles Vista's money under management was invested in Waste Energy. Correct?

A. I think I recall saying that in my testimony, correct.

Q. And you believe that to be true; correct?

A. Yes, I believe that to be true.

Q. In other words -- to make sure I understand, of all the money Charles Vista managed for its clients, 70 percent of that money was invested in Waste2Energy?

A. That is what I was led to believe.

Q. And you thought that was way too much; right?

A. Yes. And I met Gregg and Mike on that several times.

Q. You didn't think that was how a brokerage firm was supposed to run; right? You knew that?

A. Yes.

Q. And that was because it subjected the

[p.293]

brokerage clients to far too much risk. Right?

A. Yes. Absolutely.

Q. You really had no basis to say that Charles Vista would be able to find more money to pay debenture holders back; right?

A. I had no basis to say that Charles Vista...

Well, Charles Vista -- I mean, I know that Gregg Lorenzo had a couple of friends that owned small brokerage firms that were looking -- he made presentations to see if they would help raise money as a selected dealer. I don't know if that falls under the umbrella of solely, exclusively Charles Vista.

But based on what was going on with Waste2Energy and Charles Vista in October, I think it is accurate to say that Charles Vista would not have the buying power or the resources to properly fund Waste2Energy in order to repay the debentures. I think that is accurate.

Q. You knew it was wrong to send the deal point e-mails; right?

A. Yes. I know it is wrong now.

Q. You knew it was wrong at the time,

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didn't you?

A. Well, after I hit the send button and reviewed what was going on I wish I never sent it. I don't have

any history of doing this. This was just a severe oversight.

Q. So let me make sure I understand. You hit the send button and then you went back and looked at your e-mail and realized you shouldn't have sent it?

A. No, not exactly. I know that Michael Molinaro reviews all -- reviews everything. He usually retracts any e-mails that are inaccurate. I didn't see a retraction.

Well, there was just a -- there was just a lot going on at Charles Vista there, like in my testimony says. You know, it was an honest mistake. There is just a loft things going on here because of my tenure at Charles Vista and the situation that I was in at the time.

Q. Charles Vista received fees to act as the exclusive placement agent for the debentures. Correct?

A. That is correct.

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Q. It was paid about 18 percent from the proceeds of the debenture offering?

A. Correct.

A. 10 percent commission, 3 percent non-accountable expense, 5 percent investment banking fee bonus.

Q. That totals 18 percent?

A. Yes, which I received -- for the record, I received 1 percent of that.

Q. You received 1 percent of it?

A. 1 percent of the 18. Yes.

Q. Charles Vista's fees, this 18 percent, you thought that was exorbitant; right?

A. Yes. It was one of my recommendations to fix this was to reduce their fees.

Q. Gregg Lorenzo had promised to give you a cut of any of the money you raised selling debentures. Correct?

A. Any of the money I raised selling debentures? I got a 1 percent of what was raised. 1 percent of what I -- if I did recommend it and solicit it directly to my clients, I would get whatever the brokers were getting. I believe they were getting 6 or

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7 percent of the 10.

Q. They were getting 7 to 9 percent?

A. He varied it depending on the needs of the company.

Q. So Gregg Lorenzo told you you would get between 7 and 9 percent of the money you raised selling debentures. Correct?

A. Yes. To clients I was the registered rep of.

Q. During this October 2009 time period, September, October, you were focused on your work at Charles Vista. Right?

A. Well, I was asked to bring another deal in. So although -- you know, that guy Vess kind of picked up a lot of investment banking slack. Gregg asked me to train Vess. I did the best I could and -- you know, I was focused but, you know, I was also spending time on working with May Davis and Gusrae Kaplan & Bruno, who was the attorney for China Biancotang.

It was September and October when I began to work on the selective dealers agreement between May Davis and Charles Vista in American capital, another banker in the China Biancotang

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deal.

So I was involved in this whole thing but, you know, there was other things going on, started other things going on other than Waste2Energy as well.

Q. But you weren't checked out from your duties at Charles Vista?

A. Formally checked out?

Q. Mentally checked out.

A. Mentally checked out? Yeah, by September -- by September -- you know, there is a whole bunch of stuff here. By September I was financially broke.

What was going on was I was supposed to be reimbursed to pay Sara -- I paid Sara Holmes out of my own pocket and Gregg promised to reimburse me. She worked for Charles Vista, but since she came with me and Charles Vista was a start-up, they didn't have much money.

I said, "Gregg, when the company gets on their feet."

He said, "Okay, Frank, I will reimburse you for Sara Holmes:

I also was doing a commute from north

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Jersey. They wanted us to work 8 to 8. So Michael Molinaro had an apartment at Battery Park. He said, Frank, take the apartment and we'll reimburse you." But I never got reimbursed.

Come August and September I was broke. And they never reimbursed me for the money, parking, commute. I was out about close to 80,000. I only made 1 percent of the debentures. So my whole take at Charles Vista was about 110 to 120,000 and 45 of it went to Sara Holmes, 15,000 went to the second apartment, plus my own living expenses.

So, by August I was starting to go into debt and borrow money because they just said, "Frank, we just can't reimburse you right now."

So the point I am trying to make is there were other things going on. I don't want to sound -- making a cop out, but there were some other things going on at Charles Vista which leads me to believe why I made this mistake in the first place. Just very unlikely that I did something like this. I missed it.

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Q. Well, isn't it fair to say that you were proud of the work that both you and Gregg Lorenzo were doing at Charles Vista in October 2009?

A. In October?

Q. Yes. October 2009. You were proud of that work; right?

A. Proud in October 2009? I may have said that somewhere but I don't -- I can't say -- maybe earlier than that I was proud. I was proud until Sara Holmes told me, "You got to start listening to what these guys are telling the clients."

Q. When was that?

A. I can't recall but it was probably in the summer.

Q. But it is also fair to say, isn't it, that in October 2009 you thought that Charles Vista was a high quality investment bank?

A. In October 2009?

Q. Right?

A. I am sure I said it. That is why you are saying it. In October 2009. Yeah, well, I am sure if you are saying it I said it

[p.300]

somewhere. But if I said it in --

MR. HANTMAN: Let me clarify. Just because counsel asked you a question doesn't mean you have to have said it.

JUDGE FOELAK: Yes. Don't guess.

MR. JANGHORBANI: And Mr. Hantman is interjecting.

THE WITNESS: I don't know if October is the right time.

Q. I am not asking how you testified previously. I am asking, as of October 2009 is it fair to say that you were proud of the job both you and Gregg Lorenzo were doing at Charles Vista?

A. October? I know I was proud at some time. I don't know if it was October. I'd say that was late. I would say that was late.

Q. So you weren't proud of what was going on at Charles Vista by October 14, 2009? Is that what you are saying?

A. Well, proud? I think proud is a stretch.

Q. All right. And you didn't think that Charles Vista was a high quality investment bank

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in October 2009?

A. Well, it started with the right intentions but no, no, not the way it was being handled.

Q. You testified before the SEC on November 12th of 2009, didn't you?

A. Did I? I guess so. November 12, 2009 I testified?

Q. If I can ask you to turn to the transcript labeled November 12, 2009? If you look at the first page, do you see that?

A. Yes.

Q. Does that refresh your recollection that you testified before the SEC staff on November 12, 2009?

A. November 12, 2009. Yes.

Q. And you were under oath. Correct?

A. Correct.

Q. And you told the truth. Correct?

A. To the best of my knowledge.

Q. And you told the SEC staff -- you can set that document aside, sir.

You told the SEC staff, didn't you, that you were executing on your and Gregg

[p.302]

Lorenzo's vision to open up a full blown, high quality investment banking Division. Correct?

A. At the start of Charles Vista, yeah.

Q. But that is what you told the SEC staff in November 2009, isn't that right?

A. Yes, but I don't know what time frame I was referring to.

Q. As of November 2009; isn't that correct?

MR. HANTMAN: Your Honor, it is argumentative.

Q. Isn't it also the case that you told the staff in November 2009 that Gregg Lorenzo was an honest guy? Right?

A. November 2009?

Q. Yes.

A. I may have gotten my years wrong. By November 2009 there is no way on God's green earth I thought Gregg Lorenzo was an honest guy.

Q. There is no way you told the SEC staff that under oath?

A. I may have made a mistake with the time frames. By November? November 2009? I mean, I may have gotten the years wrong.

[p.303]

Q. And you testified that you still believed in the Waste2Energy deal in November 2009, didn't you? That is what you told the staff; isn't that true?

A. I told the staff that after Benkovsky made his $2 million investment I no longer believed in Waste2Energy.

MR. JANGHORBANI: Your Honor, I would like to read a couple of admissions. I am trying to speed this along. The first is in the November 12, 2009 transcript, page 203, starting at line 16.

MR. HANTMAN: What page?

JUDGE FOELAK: 203.

THE WITNESS: Okay.

MR. JANGHORBANI: May I read, your Honor?

JUDGE FOELAK: Okay.

MR. JANGHORBANI: "Question: Has Charles Vista done any investment banking deals?

"Answer. We are in the middle of working on Waste2Energy. We believe in the project. We were offered -- there was a China deal doing 108 million with 16 million net

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income. We were part of the selling group. $11 million project. We were offered to place $2 million of it so we started to bring in those high quality projects. So we do have two investment banking projects."

Q. Did I read that correctly, Mr. Lorenzo?

A. Yes, you did.

MR. JANGHORBANI: And from the same transcript, your Honor, I would like to read two more excerpts. The next is at page 22.

THE WITNESS: Same date?

MR. JANGHORBANI: Same date. November 12, 2009, page 22.

JUDGE FOELAK: Okay.

MR. JANGHORBANI: Starting at line 6. May I read, your Honor?

JUDGE FOELAK: Yes.

MR. JANGHORBANI: "Question: Of what year?

"Answer. 2008, last year. I wasn't there very long, maybe nine, ten months. And then Gregg Lorenzo -- I got along. Gregg is a bright guy, honest guy. He started the business

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very naive but he is a hard working, bright guy, very talented kid. We share the same last name; we are not related. It is circumstances. We came together and he asked me to come in and help him with Charles Vista. That is the Cliff Notes version of 22, 23 years of history."

Q. Did I read that correctly, Mr. Lorenzo?

A. Yes. Probably how I felt about him at the time, at the time he asked me to come into Charles Vista.

Q. "At the time" being November 2009 when you testified to the SEC staff?

A. No. When he asked me to -- when he went and asked me to come over to John Thomas. That is -- I think that whole thing was when we left Mercer Capital and went to John Thomas. Correct?

Q. Except your answer was all in the present tense; right?

A. Is it?

Q. "Gregg is a bright guy, honest guy." That is the present tense; right?

A. Well, I mean, by November 2009 --

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(inaudible.)

JUDGE FOELAK: Something about "there was no love lost"?

THE WITNESS: By November 2009 there was no love lost between me and Mr. Lorenzo.

Q. But you didn't tell the SEC about that; right?

A. No, but I think there is some testimony in here about falling out with Gregg Lorenzo somewhere else.

Q. Right, but on November 12, 2009, less than a month after you sent the deal points e-mails you didn't tell the staff about any problems you may have been having with Gregg Lorenzo; correct?

A. I think it wasn't asked what problems I was having with him then. It was asked how I met him back in 2008.

MR. JANGHORBANI: I would like to read a final excerpt that goes to this, your Honor. Same transcript, page 201, starting on line 7.

THE WITNESS: 11/12?

MR. JANGHORBANI: 11/12/2009, page 201, starting line 7.

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JUDGE FOELAK: Okay.

MR. JANGHORBANI: May I read, your Honor?

JUDGE FOELAK: Go ahead.

MR. JANGHORBANI: "Question: Can you tell me what you and Gregg discussed in term of what you were supposed to do at Charles Vista?

"Answer: With pride. We were going to leave these early stage companies because they exposed the firm and clients to way too much risk. It seemed like our experience where no matter how good our intentions were, it seemed like there were so many thing that can wrong with these early stage companies.

"They never seemed to hit revenue when they said they were going to. They always seemed like they were always cash poor and never seemed to have enough resources to maintain public listing, pay the accountant, the attorneys, the filings, the 8-K's.

"Our vision, and we are doing it now, is to open up a full blown high quality investment banking Division with analysts, due diligence, the right legal team and the right

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deal source, whether it be companies doing 50, 100 million in revenue with at least 12 percent profit margins, with an advisory board, certified financials, all the early stage stuff that would be done already.

"And we would take less commission and give our clients high quality projects. And we would get away from the previous world that we were in. Institutional clients, PIPE funds, hedge funds, large accredited investors and bring something to our clients that we could be proud of, that we felt it was viable and

that it would work out properly and give the client a good chance."

Q. Did I read that correctly?

A. Yes.

Q. So you didn't tell the SEC staff that you saw any problems with the way Charles Vista or Gregg Lorenzo were operating when you testified in 2009. Right?

A. In 2009 I don't recall when -- I made statements about how they were selling and how they were way too top heavy in Waste2Energy.

Q. You don't recall telling any of that

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to SEC staff when you testified in 2009?

MR. HANTMAN: I take exception to the characterization. He is asking questions -- he is not saying "As of today how do you feel about Gregg Lorenzo? How do you feel about having started a new company?"

It is true he is being questions on this day but because he is being asked questions on that day doesn't mean every question relates to how he felt about Gregg Lorenzo on that particular day.

This client may not be too articulate but clearly if this is being put in for evidentiary value it is a total distortion. Everything he says on that day is on that day. If I say to someone, "How did you meet your wife or girlfriend," and I go into it and then the question is, "On that day you met her?" I'd say, "No, of course I didn't meet her today."

JUDGE FOELAK: To shortcut this, Counsel, it seems like maybe the present tense might be used maybe ungrammatically at times.

MR. JANGHORBANI: Mr. Hantman's point is exactly the point, your Honor. On that day,

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on November 12, 2009, when asked about his feelings about Charles Vista and Gregg Lorenzo, he answered this way in the present tense. He did not say any of the things he is saying now.

MR. HANTMAN: Maybe it is confusing. "We were going to leave." Obviously, he is referring to the past.

JUDGE FOELAK: He did read -- not to get into it. "And we are doing it now."

Anyway --

MR. JANGHORBANI: It says what it says, your Honor.

Q. Now, you didn't leave Charles Vista until February 2010. Right?

A. That's correct.

JUDGE FOELAK: Counsel, when you come to a good breaking point it might be not a bad idea to break.

MR. JANGHORBANI: I have one more very short line of questioning that may help to wrap this up.

JUDGE FOELAK: It may? Okay.

MR. JANGHORBANI: I will strive not to go back to testimony.

[p.311]

Q. After you left Charles Vista you continued to work in finance. Correct?

A. Correct.

Q. You became senior vice president of investment banking at American Capital Partners?

A. Yes, I did.

Q. At some point you started working a Hunter Wise Financial?

A. Yes, I did.

Q. When did you start that?

A. I believe it was November 2010.

Q. And Hunter Wise is an investment bank?

A. Private equity, M and A. No accredited -- no individual clients, hardly any.

Q. You are a managing director?

A. Yes.

Q. You primarily focus on funding private and public companies?

A. Not lately. Mostly private equity groups and hedge funds and institutional financing. Every now and then a public deal, public company needs financing. Anyhow, that is primarily where I am at.

Q. So it is not accurate to say you

[p.312]

primarily focus on the funding of private and public companies?

A. Yeah. I'd say that's accurate. It is a different profile but -- than Charles Vista, but it is accurate.

Q. You are still at Hunter Wise?

A. Yes.

MR. JANGHORBANI: This is a good time to break, your Honor.

JUDGE FOELAK: Very good.

You can resume your place in the audience.

Do you have any idea how much longer you will be tomorrow?

MR. JANGHORBANI: I think very, very little, your Honor. If you give me one second I can give you a better sense.

(Pause.) Really probably just a couple of minutes.

JUDGE FOELAK: Mr. Hantman, do you have a guesstimate as to -- a guesstimate?

MR. HANTMAN: I would try to get through this in like two hours, two and a half hours.

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JUDGE FOELAK: Okay. Just asking.

MR. HANTMAN: It depends whether I am going to go through all these transcripts and just pick out the page and line and read it into the record and say to the witness, "On such and such day did you say," page and line and let him read it into the record.

JUDGE FOELAK: I would suggest that perhaps you consider, even if it is after the hearing, conveying your designations to the Division and seeing if they have any counter-designations and putting them in then.

MR. HANTMAN: I would prefer that. I think it will save time and I don't need the dramatization by putting out two or three lines of something, though counsel has done an excellent job and I commend him.

MR. JANGHORBANI: Again, your Honor, I don't know which witness he is speaking about specifically but assuming it is his client --

JUDGE FOELAK: I am sure it is.

MR. JANGHORBANI: I will object to him putting in his own client's testimony. It is classic hearsay when used by that witness for

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that witness. He is not unavailable.

JUDGE FOELAK: For all I know he is going to put in the ten lines before your questions, to put it in context. That is only fair.

MR. JANGHORBANI: If he is putting it in for contextual purposes we may be able to talk about it. But if he is putting it in for the truth of that statement

we will have a problem with it. Maybe the best way is for us to talk about it and see where we end up.

MR. HANTMAN: That is a good idea.

JUDGE FOELAK: Okay. Very good. Ten o'clock tomorrow.

MR. HANTMAN: Your Honor, if you don't mind, I had a prior engagement. Would it make much difference if we started at 10:30 tomorrow? We won't be going beyond tomorrow anyway.

JUDGE FOELAK: It's okay with me.

MR. JANGHOBANI: No objection.

JUDGE FOELAK: All right. 10:30.

(Time Noted: 5:19 p.m.)

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SCOPIST CERTIFICATE

I, JOYCE THOMPSON, hereby certify that the foregoing transcript consisting of 315 pages is a complete, true and accurate transcript of the investigative hearing, held on Wednesday, September 18, 2013, at 3 World Financial Center, New York, New York, in the matter of GREGG C. LORENZO, FRANCIS V. LORENZO, and CHARLES VISTA, LLC.

I further certify that this proceeding was reported by DEBRA STEVENS and that the foregoing transcript has been scoped by me.

_____ _____

JOYCE THOMPSON Date

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UNITED STATES SECURITIES AND
EXCHANGE COMMISSION
REPORTER'S CERTIFICATE

I, DEBRA STEVENS, Repoter and Notary Public hereby certify that the foregoing transcript of 315 pages is a complete, true, and accurate transcript of the testimony indicated, held on September 18, 2013, at the Securities and Exchange Commission, 3 World Financial Center, New York, New York, in the matter of: GREGG C. LORENZO, FRANCIS V. LORENZO, and CHARLES VISTA, LLC.

I further certify that this proceeding was reported by me and that the foregoing transcript was prepared under my direction.

_____ _____

DEBRA STEVENS Date

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PROOFREADER'S CERTIFICATE

In the Matter of:	GREGG C. LORENZO, FRANCIS V. LORENZO, and CHARLES VISTA, LLC,
File Number:	3-15211
Date:	September 18, 2013
Location:	3 World Financial Center New York, New York

This is to certify that I, DEBRA STEVENS, the undersigned, do hereby swear and affirm that the attached proceedings before the United States

Securities and Exchange Commission were held according to the record, and that this is the original, complete, true and accurate transcript that has been compared to the reporting or recording accomplished at the hearing.

_____ _____

DEBRA STEVENS Date

UNITED STATES OF AMERICA
SECURITIES AND EXCHANGE COMMISSION

Administrative Proceeding File No. 3-15211

In the Matter of GREGG C. LORENZO, FRANCIS V. LORENZO, and CHARLES VISTA, LLC, Respondents.	))))))

26 Federal Plaza
Courtroom 238
New York, New York

September 19, 2013
10:31 a.m.

BEFORE: CAROL FOX FOELAK,
Administrative Law Judge

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APPEARANCES:

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ALSO PRESENT:

Raymond Chan, Paralegal
Kelly Taddonio, Law Clerk
Frank Lorenzo, Respondent

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PROCEEDINGS

JUDGE FOELAK: Good morning.

MR. JANGHORBANI: One procedural issue before we recall Mr. Lorenzo to the stand.

We thought about your Honor's advice yesterday about Mr. Lorenzo's testimony transcript, and we have agreed instead of going back and forth on designations and cross-designations, the parties will stipulate to just mark the entirety of his July 2012 transcript as an exhibit.

JUDGE FOELAK: That sounds good. I mean, it is not that long.

MR. JANGHORBANI: No, it is not that long. If that is acceptable to your Honor, I will just go ahead and have one marked.

JUDGE FOELAK: Okay. That will be Exhibit –

MR. JANGHORBANI: It would be Division 132, just keeping with the numbering we have now, not that there will actually be 132 exhibits.

JUDGE FOELAK: So Division Exhibit 132 consisting of Frank Lorenzo's July 26, 2012 investigative testimony is admitted.

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(So received in evidence as Division Exhibit 132.)

MR. JANGHORBANI: Your Honor, would you like me to hand up a marked version?

JUDGE FOELAK: Okay. Thank you.

MR. JANGHORBANI: The Division then recalls Mr. Lorenzo to the stand.

JUDGE FOELAK: I would like to remind you you are still under oath from yesterday.

Whereupon,

FRANCIS LORENZO,

having been previously duly sworn/affirmed, was examined and testified further as follows:

THE WITNESS: Can I bring this?

JUDGE FOELAK: Certainly.

THE WITNESS: Thank you.

MR. JANGHORBANI: May I proceed, your Honor?

JUDGE FOELAK: Yes.

CONTINUED DIRECT EXAMINATION

BY MR. JANGHORBANI:

Q. Morning, Mr. Lorenzo.

A. Good morning.

Q. Toward the end of the day yesterday

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you testified that you were proud of the work at Charles Vista until Sera Holmes told you about some of the things that the brokers had been saying to clients. Do you recall that?

A. Yes, I do.

Q. And that was in about the summer of 2009?

A. Late, late summer.

Q. So Ms. Holmes told you something that made you no longer proud to work at Charles Vista. Correct?

A. I'd say that's accurate.

Q. She told you that there was something wrong going on at Charles Vista. Right?

A. Yes.

Q. What did she tell you?

A. She said the brokers are not being a hundred percent accurate in their presentations.

Q. And that would include Gregg Lorenzo. Correct?

A. I would imagine so, yes.

Q. What specifically did she tell you about inaccuracies that the brokers were making in their representations to clients?

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A. I don't recall her being specific with any -- with any -- any items or any -- any statements. It was just kind of an overall statement that it was very high pressure and they seemed like they are stretching the truth. I think she used the words "stretching the truth."

Q. And did you ask her for specifics?

A. No, I don't recall that I did.

Q. So you didn't want to know how the brokers at Charles Vista were stretching the truth to their clients?

A. Well, you know, I knew that they were doing high pressure sales, standing up and overcoming objections but, you know, I did talk to Molinaro and Gregg about the statements about the collateral. I remember telling them, sitting them down saying, "Be careful what you say about the asset in your presentation backing up the debentures because it is not -- it is not formally -- it is not formal collateral. There is no UCC filed against that asset."

Q. I want to understand this conversation with Ms. Holmes a little bit better, though.

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So Ms. Holmes had told you something about the brokers, including Gregg Lorenzo, stretching the truth in their presentation to the clients. Right?

A. Yeah, if I recall correctly, something like that.

Q. That is what you just testified to. But you didn't ask her for any further specifics?

A. I don't -- I don't remember.

Q. You don't remember asking her for specifics?

A. No.

Q. And that is because you didn't want to know -- you didn't want to know what was going on, did you?

A. No, that is not accurate. I mean, I did speak to Mike and Gregg about the sales practices.

Q. Now, you have been mentioning a Mike. I think his name has come up a couple of times through the last couple days. That is Michael Molinaro. Is that correct?

A. Yes, that's correct.

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Q. He was Charles Vista's compliance officer. Right?

A. Correct.

Q. His job was strictly compliance. Right?

A. As far as I knew, yes.

Q. And you didn't have much substantive discussion with Mr. Molinaro about Waste2Energy, did you?

A. He was in all the meetings with me and Gregg most of the time.

Q. Well, you don't recall having much tangible discussions with Mr. Molinaro about Waste2Energy, do you?

A. You know, I am trying to remember. I know he was a -- I'd say he was in at least 50 percent of the meetings and he was -- I remember there was a whole bunch of investors came up from Waste2Energy. He was in that meeting as well. And he was in the presentation meetings to the brokers in the morning when Waste Energy would come up.

Q. You recall you testified before the Commission on July 26, 2012. Right?

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A. Yes.

Q. You testified about that yesterday. Correct?

A. Yes, I did.

Q. And you told the truth during that testimony?

A. The truth as I know it at that time, yes.

MR. JANGHORBANI: Your Honor, I would like to read from page 25 of that transcript.

JUDGE FOELAK: Okay.

MR. JANGHORBANI: Starting at line 25.

THE WITNESS: What date was that?

MR. JANGHORBANI: The July 26, 2012 transcript, page 25, starting at line 25.

May I read, your Honor?

JUDGE FOELAK: Yes.

MR. JANGHORBANI: "Question: Generally what did you speak to Mr. Gregg Lorenzo about?

"Answer: The corporate finance obligations of Waste2Energy.

"Question: And what about Mr. Molinaro, same question?

[p.328]

"Answer: Looking back I don't know if there was much substantial tangible discussion with Molinaro. I don't recall."

Q. Did I read that accurately Mr. Lorenzo?

A. Yes, you did.

MR. JANGHORBANI: Mr. Chan, can I ask you to pull up Division 35?

Q. Do you have that on your screen, Mr. Lorenzo?

A. Yes, I do.

Q. Do you see that says background questionnaire for Francis V. Lorenzo?

A. Yes.

Q. You see there is handwriting on these pages?

A. Yes.

Q. That is your handwriting. Correct?

A. That is correct.

Q. You filled out this form?

A. Yes, I did.

MR. JANGHORBANI: Your Honor, I would like to move the admission of Exhibit 35.

JUDGE FOELAK: Exhibit 35 is admitted.

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(So received in evidence as Division Exhibit 35.)

Q. You filled this out truthfully and accurately?

A. Yes, I did.

Q. You can set that document aside.

You recall yesterday we spent some time discussing the $10 million in intangible assets?

A. Correct.

Q. And we spent some time discussing how you had communicated with Waste2Energy about the status of that asset over the summer and fall of 2009. Do you recall that?

A. How I communicated about the status of that asset? Do I recall -- I don't recall that.

Q. Fair enough.

MR. JANGHORBANI: Mr. Chan, can I ask you to pull up Division 27?

Q. Do you have that on your screen, Mr. Lorenzo?

A. Yes, I do.

Q. You see that is an e-mail from Francis Lorenzo to a number of people?

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A. That's correct.

Q. Dated April 29, 2009. Correct?

A. Yes.

Q. You sent this e-mail in April 2009. Correct?

A. Yes, I did.

Q. And you sent it to Chris Taylor and Peter Bohan. Correct?

A. Yes.

Q. A number of other people are cc'd right?

A. Correct.

Q. Mr. Taylor and Mr. Bohan were at Waste2Energy. Right?

A. That is correct.

Q. You write down in the body, you say -- well, before I get there, the subject matter is "Intangibles"?

A. That is correct.

Q. So you are talking about the intangible asset --

A. Yes.

Q. -- of Waste Energy; correct?

A. Yes.

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Q. The $10 million we spent a lot of time talking about?

A. Yes.

Q. You write at the bottom "On the part asset part of the FS." You see that?

A. Yes, I do.

Q. You mean financial statement there?

A. Yes, I do.

Q. The next page you write approximately 10 million of the approximate 12 million is intangibles. Do you see that?

A. Correct.

Q. Then you say "Can someone tell me what this is?" You see that?

A. Yes.

Q. It is fair to say in April 2009 you were asking Waste2Energy about this 10 million intangible asset. Right?

A. Yes, that is correct.

Q. You can set that document aside, sir.

MR. JANGHORBANI: Your Honor, I offer Exhibit 27.

JUDGE FOELAK: Exhibit 27 is admitted.

(So received in evidence

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as Division Exhibit 27.)

MR. JANGHORBANI: Mr. Chan, can you pull up Division 66?

Q. Mr. Lorenzo, you see this is a Form 8-K of Waste2Energy's?

A. Yes.

Q. The date of the report is September 21, 2009. Correct?

A. Correct.

Q. If you turn to the next page you see it is signed by Craig Brown?

A. Yes.

Q. It is dated September 22, 2009. You see that?

A. That is correct.

Q. So it is fair to say that Waste2Energy filed this Form 8-K on September 22, 2009?

A. That is correct.

Q. Fair to say you read this document?

A. Yes, I probably -- I skimmed it. I'd say that's correct.

Q. You see the first line under item 3.01 it says that FINRA had notified Waste2Energy Holdings, Inc. that on August 20, 2009 that it's

[p.333]

delinquent in filing its 10-Q for the period ended June 30, 2009. Do you see that?

A. Yes.

Q. And that is the 10-Q we talked about yesterday, right?

A. We talked about a few 10-Q's.

Q. The 10-Q where the company reported its June 30th unaudited numbers?

A. The October 1st filing?

Q. Yes.

A. Yes, correct.

Q. The 10-Q that included the audited numbers as well. Correct?

A. Correct.

Q. You knew on September 22, 2009 that Waste2Energy was delinquent in getting its auditeds filed, right, its audited numbers?

A. I think I was -- the date this was filed was September 21st, correct.

Q. It says dated September 22, 2009. You see that?

A. Yes. So I found out about this then.

Q. Okay. But it is fair to say that on September 22, 2009 you knew that Waste2Energy

[p.334]

was delinquent in filing its audited numbers. Right?

A. Yes.

Q. You can set that document aside, sir.

MR. JANGHORBANI: Your Honor, I offer Division 66.

JUDGE FOELAK: Exhibit 66 is admitted.

(So received in evidence as Division Exhibit 66.)

MR. JANGHORBANI: May I have one minute of the Court's indulgence?

JUDGE FOELAK: Certainly.

MR. JANGHORBANI: Thank you.

(Pause.)

MR. JANGHORBANI: I have nothing further, your Honor.

JUDGE FOELAK: Very good. Cross.

MR. JANGHORBANI: One question, your Honor. Is this going to be Mr. Hantman's entire examination of Mr. Lorenzo? That is to say is he going to do direct and cross, or does he plan on recalling him in their case in chief.

JUDGE FOELAK: Well, I think that should be Mr. Hantman's option.

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MR. HANTMAN: What do you prefer?

MR. JANGHORBANI: We don't have any other witnesses, so I think it --

JUDGE FOELAK: I guess he wants to know -- theoretically, if you had, quote/unquote, cross-examination and he had redirect or something, then he would rest, whereas if you do the whole thing at once, which may be more convenient to you, then the point at which he rests is --

MR. HANTMAN: I would have no problem if the government wants to rest.

MR. KAUFMAN: We are not resting now, your Honor. We are just wondering if it will be done all at once. We are not resting now. We would want a break before we rest to make sure we have got everything in.

We are wondering if this would be more efficient for this to be done all at once. That is all. If it isn't, fine.

MR. HANTMAN: If it is more efficient for your Honor and the SEC, I will combine the two.

JUDGE FOELAK: Okay. What were you

[p.336]

planning to do?

MR. HANTMAN: I was going to do both but I might as well just stay with this witness --

JUDGE FOELAK: It probably would be more efficient.

MR. HANTMAN: Okay.

CROSS/DIRECT EXAMINATION

BY MR. HANTMAN:

Q. Mr. Lorenzo, you have been in the investment banking business for how many years?

A. Investment banking?

Q. Yes.

A. Since 1993.

Q. During that period of time, prior to this situation, had you ever been accused of fraud?

A. No.

Q. Had you ever been accused of making any misrepresentations?

A. No.

Q. Have you ever had any clients of yours sue you in FINRA for making material misrepresentations or trying to defraud them?

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A. No.

Q. Have you ever been a party to any lawsuits, civil lawsuits where you were alleged to have defrauded people?

A. No. However, there is a pending FINRA matter with a debenture holder, a client of Gregg Lorenzo's, in which I was named. That hasn't been resolved yet.

Q. Does that relate to W2Energy?

A. Yes. It is the same -- it is the debentures.

Q. And that has not been resolved yet?

A. No.

Q. Do you have your FINRA report here today?

A. Yes. I printed it out last night.

Q. This is a public record of any disciplinary actions with FINRA?

A. Correct.

Q. This is available on the internet?

A. Finra.org.

Q. It is a public record?

A. Yes, it is.

MR. HANTMAN: Obviously, the

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government is aware of this FINRA report. I would ask the Court to take judicial notice. I have a hard copy here. Unfortunately, I don't have a copy for the government but I would like to put this in evidence, your Honor, or at least let the Court take judicial notice of it.

JUDGE FOELAK: I am not sure I can take judicial notice of it.

MR. JANGHORBANI: Your Honor, this wasn't on their exhibit list. We don't have a copy of it. I am at

a little bit of a loss. Normally I wouldn't object to a CRD FINRA report being put in. I think we are at least entitled to have a copy of it to follow along.

JUDGE FOELAK: Why don't you give him your copy.

MR. JANGHORBANI: Thank you. Is this being marked as an exhibit?

MR. HANTMAN: It will be marked. Do you want me to have it marked first?

MR. JANGHORBANI: Well, I think it needs to be in the record.

MR. HANTMAN: It will be Respondent's Exhibit 1.

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MR. JANGHORBANI: May I take a second to look at it before it goes in to make sure it is what I think it is?

JUDGE FOELAK: Certainly.

(Pause.)

MR. JANGHORBANI: We don't have an objection to putting in Respondent 1.

JUDGE FOELAK: Respondent Exhibit 1 is admitted.

(Respondent Exhibit 1 received in evidence.)

MR. HANTMAN: Thank you.

Q. Other than this proceeding here, have you ever been accused of sending out e-mails to people with information that was false or a misrepresentation?

A. No.

Q. Excuse me?

A. No.

Q. Have you ever been part of like a conspiracy for like major Wall Street people to defraud people through the use of e-mails?

MR. JANGHORBANI: I will object to the question. One, conspiracy calls for a legal

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conclusion. Two, major Wall Street people? I don't really know what that means. And it is cumulative of the questions he has already asked.

JUDGE FOELAK: I will overrule your objection. He can go ahead and answer.

A. No.

Q. You mentioned in the e-mails to these two different people it was at the -- I believe it was at the recommendation or at the request of Gregg Lorenzo that you were sending these e-mails out. Is that correct?

A. That is correct.

Q. Did he pay you to send these out or give us some of the flavor as to -- let's say on October 14, 2009, do you recall that day?

A. Briefly, yes.

Q. Where were you living at the time?

A. I think by then I gave up Mike Molinaro's apartment and was living in Westwood, New Jersey.

Q. How did you get to work?

A. I'd drive.

Q. Excuse me?

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A. Sometimes I'd drive, sometimes I'd take the bus.

Q. So you'd drive to work that day. Where were your offices that day?

A. 100 Williams Street.

Q. When you got to the office can you describe, if you can, what happened at the office that morning?

A. Probably -- you know, I don't recall anything specific. A typical day at Charles Vista. There is a morning meeting, I believe at 8:30 or 9 o'clock led by Gregg Lorenzo. If Michael Molinaro had any compliance news he would speak at the morning meeting.

Kind of a motivational meeting in the morning. And then -- you know, I was asked to send out these two e-mails. So Gregg gave me --

Q. Well, wait a second. These were sent out at 3:37 p.m., so let's go before that. At this meeting that you had, who was at this meeting?

A. All the brokers.

Q. Was there any discussion that you were going to be called upon to send out at Gregg

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Lorenzo's request --

MR. JANGHORBANI: Objection.

Q. -- e-mails to certain people?

MR. JANGHORBANI: He is leading the witness.

JUDGE FOELAK: You really shouldn't be leading the witness. He is your own client.

Let me ask you, where does the 3:37 come from? Is it written on the thing or is it in Greenwich mean time or --

MR. HANTMAN: It is on the e-mail.

JUDGE FOELAK: Okay. Thank you.

Q. At this meeting was the subject matter of these two e-mails discussed at all?

A. I don't recall these two e-mails being discussed in the morning meeting.

Q. Were they discussed at any time prior to 3:37 p.m. with you and anybody else?

A. Not that I recall.

Q. With respect to these two individuals, had you ever met W.S. Rothe?

A. No.

Q. Do you know who that person is?

A. Now I do.

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Q. Well, then did you know?

A. No. I assumed he was a client of Gregg Lorenzo's.

Q. Had you ever spoken to him?

A. No.

Q. Had you ever looked at any of his private placement memorandum?

A. No.

Q. Did you know how much money he had?

A. No.

Q. And the other person that got the e-mail, did you know who that person was?

A. If it is the same guy, I remember him a couple of months ago because Gregg Lorenzo wanted to open up a branch office in Central America, and I believe this guy came from Central America. So I met him for, I think, a meeting to talk about that.

Q. Were you friends with either of these people? Were you friends with them?

A. With the guy from Central America?

Q. Yes.

A. No.

Q. Or Rothe?

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A. No.

Q. Had you ever socialized with them?

A. No.

Q. Did either of them look at you as somebody who they relied upon for your advice?

MR. JANGHORBANI: Objection. Two counts. One, now he is asking the witness to testify what was in the head of Mr. Rothe and Mr. Goolcharan, if they viewed him as someone to rely on, so it is objectionable on that front.

Two, as the Court has reminded respondent, reliance is not an element of a Commission action.

JUDGE FOELAK: Yes. Your objection is sustained.

Q. As I understand it, the government's position is that these fraudulent statements were sent out ostensibly so these people would make an investment.

MR. JANGHORBANI: Objection. Once again he is leading or at a minimum he is editorializing. There is no question in here.

JUDGE FOELAK: True.

Q. Well, when Gregg Lorenzo asked you to

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send these out, did he indicate to you why he wanted these sent out?

MR. JANGHORBANI: Objection. Lack of foundation that Mr. Gregg Lorenzo asked Francis Lorenzo to send out the e-mail.

JUDGE FOELAK: Yes. It seems to me the witness testified that there was no discussion before sending out the e-mail.

Q. But did he ask you to send this out?

A. Yes.

Q. And did you ask him why?

A. I don't -- I don't remember if I -- I remember getting -- getting the e-mail addresses from him and then cut and pasting this -- this thing and sent it.

Q. Before you sent it out, did you study it in depth?

A. No.

MR. JANGHORBANI: Again, objection. He is leading his witness.

MR. HANTMAN: That is yes or no, did you study it in depth?

MR. JANGHORBANI: It suggests the answer.

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JUDGE FOELAK: It does suggest. Anyway, go ahead and answer.

A. What was the question?

Q. Can you describe, when Gregg Lorenzo asked you to send these out, okay, what, if anything, did you do before you sent it out?

A. What, if anything, did I do before I sent it out? Unfortunately, not much. I just -- I sent it out.

Q. Approximately how much time transpired between the time he told you to send these out and the time you sent it out?

A. Right away.

Q. A minute? Two minutes?

A. As soon as -- you know, he gave me the e-mail address, I typed it into the "to" column and cut and pasted this -- the content and sent it out.

Q. Did you do it in a rush, or did you like take your time?

A. Like any other e-mail. You know, I know now based on what the content of the e-mail is and what happened here that I should have never sent the e-mail out, but, you know,

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obviously -- you know, I don't want to minimize the severity of it but, you know, I just didn't give it much thought at the time. My boss asked me to send these e-mails out and I sent them out.

Q. And after you sent them out, did you have any meeting with anyone in which you discussed -- had any discussions concerning these e-mails?

A. No.

Q. Later in the day, did you check your e-mails to see whether these people got back to you and said "Frank, thanks for this information"?

MR. JANGHORBANI: Objection. He is leading his witness again.

JUDGE FOELAK: It seems like just moving the story along to a certain extent.

Q. You can answer.

JUDGE FOELAK: You can answer.

A. I check my in-box all the time. I didn't see anything from them but I wasn't specifically looking for a response from them.

Q. When you didn't get a response from

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either one of them, did you follow up?

A. No. It wasn't my place to follow up.

Q. Why didn't you follow up?

A. They weren't my clients.

Q. Well, when a week or two went by, were you curious why they didn't respond to you?

A. I figured their registered rep was handling it. The people they were speaking to at Charles Vista.

Q. Who was the rep of either one of them if you recall?

A. Either Adam Spiro or Gregg Lorenzo.

Q. Did you have any discussions with them concerning whether these two recipients of these e-mails had gotten back to anybody?

A. None that I can recall.

Q. Subsequent to sending out these e-mails, did anyone ever approach you, ever approach you to discuss whether or not these people had responded?

A. There was no – no discussion other than – other than him asking me to send these e-mails out?

Q. When was the first time that the

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subject matter of these two e-mails came up?

A. When I testified.

Q. Excuse me?

A. When I testified with the SEC.

Q. When you say you testified before the SEC, maybe give us some background there. When did you first testify for the SEC?

A. I don't remember. I don't have the dates memorized.

JUDGE FOELAK: Let the record reflect that the witness has reached for a volume entitled "Testimony transcripts" that contains a number of tabs.

A. 11/12/2009 was the first testimony.

Q. And do you know what the caption of that matter was?

A. Mercer Capital.

JUDGE FOELAK: The witness is reading from the front page of that testimony.

Q. What exhibit is that? Is that an exhibit?

A. It is testimony transcripts.

Q. Do you know what the nature of that proceeding was about?

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A. Mercer Capital.

Q. Did the SEC call you, or did you call them?

A. They sent me a letter, I believe.

Q. Do you recall what the letter said?

A. "You are required to testify."

Q. And did you have any idea at the time it was to testify about these two e-mails?

A. No.

Q. The date of that was when?

A. 11/2009. 11/12/2009. That was the first one.

Q. Were you asked any questions about these two e-mails then?

A. I don't believe so, no.

Q. And did you have a lawyer then present?

A. Yes. I believe it was Dave Gann.

Q. Did you have any understanding what the nature of this proceeding was about?

A. Potential improprieties at Mercer Capital.

Yes, David Gann was my attorney then.

JUDGE FOELAK: Let the record reflect

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the witness was reading from the front page of the document.

Q. You say it had to do with an investigation of Mercer Capital. Did Mercer Capital have anything to do with W2E at that time?

A. Mercer Capital was the banker that did -- was the brokerage firm that did an equity round in 2007 or 2008.

Q. At that time you were working for Mercer Capital?

A. Yes.

Q. So you weren't even working for Charles Vista at the time?

A. There was no Charles Vista at the time.

Q. What was the second time --

MR. JANGHORBANI: Your Honor, I have to object. I believe that Mr. Hantman is asking the witness about the November 12, 2009 testimony transcript, in other words three weeks after Mr. Lorenzo sent this e-mail when he was working at

Charles Vista. He's already testified to that earlier so I think the record

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needs to be clarified on that point.

JUDGE FOELAK: Mr. Hantman?

MR. HANTMAN: I am just asking him questions. If there is going to be some redirect that is fine.

Q. Does it refresh your memory that at the time you were working for Charles Vista?

A. In 2000 --

JUDGE FOELAK: Apparently the witness was testifying that at the time of the events in question at Mercer Capital, that was before Charles Vista had been formed. Is that correct, Mr. Lorenzo?

THE WITNESS: I believe that is correct, yes.

MR. HANTMAN: That is his testimony.

Q. Was there a second time you testified before the SEC?

A. Yes. 12/16/2009.

JUDGE FOELAK: Let the record reflect the witness again is reading from the transcript.

Q. What was the caption of that matter?

A. Mercer Capital.

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Q. Were you a respondent? Were you named in that caption?

A. No. It says witness, Frank Lorenzo.

Q. Were you asked questions then about these two e-mails in question if you recall?

A. I don't recall at this testimony, no.

Q. And did you have a lawyer present?

A. David Gann, yes.

Q. Was there a third time that you testified before the SEC?

A. Yes. On 3/18/2010.

Q. What was the nature of that proceeding?

A. Mercer Capital. And Marc Ross was my attorney.

Q. Were you a respondent in that action?

A. No –

MR. JANGHORBANI: Objection, your Honor. Lacks foundation. This is investigative testimony. There are no respondents.

JUDGE FOELAK: Good point. Again, the witness is reading from the cover page, and the cover page states file number and gives some investigative number and Mercer Capital, of

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course.

Q. Did you testify voluntarily at the time?

A. They sent me a letter, I showed up.

Q. And you cooperated?

A. To the best of my ability, yes.

Q. And you were forthright and honest with the SEC?

A. I believe I was.

Q. And did there come a fourth time that you were interviewed?

A. Yes.

Q. And when was that?

A. 7/26/2012.

Q. Did you have a lawyer present at that time?

A. No. I couldn't afford one at that time.

Q. Excuse me?

A. No. I. No. I couldn't. It was getting to be too much money to keep paying lawyers for this. Couldn't afford it at the time.

Q. So you went on your own?

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A. Yes.

Q. Did anybody prepare you for your testimony, go over the subject matter of the questions you would be asked?

A. No.

Q. Did anyone from the SEC suggest that you really should get a lawyer, it would be in your best interest?

MR. JANGHORBANI: Objection. First of all, it is hearsay what somebody else from the SEC said. Second of all, I am really not sure what the relevance is to the facts at issue in the case.

JUDGE FOELAK: Mr. --

MR. JANGHORBANI: It is also assuming facts not in evidence. In fact, the transcript says what it says, and it says the opposite of the suggestion that the question is drawing.

Q. At that point, when you were asked questions about these two e-mails, had you prepared -- had you prepared yourself beforehand to answer questions about these e-mails?

A. No.

Q. Had you done any preparation in

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anticipation of this fourth interview?

A. No.

Q. You were asked the question on page 138, between lines 18 and 25, you were asked "Can you tell

me whether you sent these e-mails, these two e-mails on those dates?"

Your response was "Yes, I sent them."

You were honest about having sent them, were you not?

A. Yes.

Q. Other than yourself, were there any other witnesses to you having sent these e-mails?

A. Not that I can recall.

Q. And at the time that you said you sent them, did you believe that you had done something wrong?

A. At the time? No. I missed it.

Q. And you were asked the question "Why did you send this individual this e-mail?" and your answer was, "I don't know."

MR. JANGHORBANI: Your Honor, at a minimum can Mr. Hantman direct us to a page? He appears to be reading from a transcript.

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MR. HANTMAN: It is page 138. Bear with me. I am sorry. It is page 139, line Number 13.

Q. You were asked the question "Why did you send this individual this e-mail, referring to the person in the Caribbean?

Do you see that?

A. Yes.

Q. And your answer was "I don't know."

A. I see that.

MR. JANGHORBANI: Your Honor, first of all, I am not sure where Mr. Hantman is going simply reading the transcript back to his client. But if he is going to do that he needs to read it accurately. The answer is "I don't know. It is obvious I sent it."

MR. HANTMAN: Well, I am not finished, your Honor.

JUDGE FOELAK: Keep reading, then. Well, you don't have to, I guess, now that it has been read by Mr. Janghorbani.

Q. Then your answer was "I don't know." Right?

A. Correct.

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Q. You are referring to that you don't know why you sent it?

A. "Why did you send this individual this e-mail?"

"I don't know. It is obvious that I sent it."

Q. You are saying it is obvious that you sent it but it doesn't explain whether you knew why you sent it or not?

MR. JANGHORBANI: Once again, your Honor, Mr. Hantman is leading. He is dictating to the witness what his responses should be. If he has open-ended questions to ask in a direct fashion he needs to ask those questions. I object to this.

Q. After you said "I don't know" you said, "It's obvious I sent it."

What was obvious?

A. That I sent this -- this guy from the Caribbean an e-mail on behalf of Gregg Lorenzo.

Q. Then you were asked the question, on page 141 -- let me forget that a second, okay? Let's go into this other question.

You were asked the question "At the

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time did you know these statements were inaccurate and misleading?" Do you recall that?

MR. JANGHORBANI: Can we get a page number, your Honor?

MR. HANTMAN: I won't even refer to that.

Q. Do you recall whether you were asked the question whether these e-mails were misleading and inaccurate?

A. Yes.

MR. JANGHORBANI: Once again, if all he is doing is asking do you recall a very specific thing, it is a leading question. If he is going to direct us to something he needs to direct us to something. I object to the framing of the question without a transcript cite.

JUDGE FOELAK: Mr. Hantman, you are sort of like reading from the transcript. Does it matter whether he recalls now whether he said that? Maybe

just speed it up by referring us to the transcript if you want to.

MR. HANTMAN: I will get back to that, your Honor.

Q. Now, Mr. Lorenzo, I refer you to

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Defendant's Exhibit 65 if you take a look at the book a second.

JUDGE FOELAK: Division Exhibit 65?

MR. HANTMAN: Yes. It is in the book as Defendant's Exhibit 65.

JUDGE FOELAK: 65, which is in evidence.

MR. KAUFMAN: We'll put it on the screen.

A. Yes, I got it.

Q. This appears to be a list of all the debenture holders. Is that correct?

A. That's correct.

Q. And these are people who had already put -- had already, you know, put money into W2Energy. Is that correct?

A. That's correct.

JUDGE FOELAK: Wait a minute, Mr. Hantman. Let me ask you to ask him a clarifying question. What do you mean by "already put money in?" Existing equity holders or what?

MR. HANTMAN: Good point, your Honor.

Q. Maybe you can explain, on the second

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page, starting with Gary Ash, do you see that at the top?

A. Got it.

Q. It says "Noteholders," does it not?

A. Correct.

Q. What does that refer to?

MR. JANGHORBANI: I am going to object to this, your Honor. Lack of foundation. He is not on this e-mail. He didn't write it, there is no basis -- he hasn't said he's ever seen it before. He can't know what this means.

JUDGE FOELAK: Where are you going with this, Mr. Hantman?

Q. Well, have you ever seen this before, this list?

A. Yeah, when I reviewed the evidence.

MR. JANGHORBANI: So he's seen it after the fact. He has no personal knowledge about what this list means. If Mr. Hantman wants to make an argument from it, he can do that on his closing.

JUDGE FOELAK: Well, let's see where Mr. Hantman is going with it.

MR. JANGHORBANI: Thank you, your

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Honor.

Q. Well, at the time you sent out these two e-mails to these two individuals, were you aware of other people who had already had notes in W2Energy?

A. Yes, of course.

Q. And did you send any of these e-mails to any of these other people?

A. No.

Q. When I say "other people," people who had already made investments or had purchased notes in the company. Correct?

A. Correct.

Q. Is there any reason why, with people who had already shown a commitment to this company, why didn't you send them this e-mail?

MR. JANGHORBANI: Objection. I don't -- vague.

JUDGE FOELAK: Well, maybe he knows -- maybe it is not vague.

MR. KAUFMAN: Is the suggestion that Mr. Goolcharan had already invested at the time the October 14th e-mail was sent out? Because that is contrary to the record.

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MR. HANTMAN: That is not the question.

JUDGE FOELAK: Just one attorney, please.

Q. The question is, at the time that you sent these e-mails out, were you aware of people who had already made some equity or invested money in W2Energy?

A. Yes, I was.

Q. Is there any reason why you did not send e-mails to any of these other people?

JUDGE FOELAK: Let the record reflect that the witness is sort of gesturing in a "who knows" fashion.

A. I don't know why I would. These aren't my clients. I hardly spoke to any of them. Never solicited or presented Waste Energy to any of these people.

By being at Charles Vista I started recognizing some of their names as a noteholder. But having a relationship or a dialogue or an interaction with any of them, it was all for updates or after the fact, after they made their investment.

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Q. But when you were at Charles Vista, did you have e-mail addresses of these different noteholders?

A. No. Well, some of them I did, but -- no. I mean, why would I? I didn't know their e-mail addresses.

Q. Well, is there any reason why you couldn't have -- since you had this letter, any reason why you couldn't have just sent this e-mail to like 500 people?

A. Well, now, this letter is the center of my universe but at the time I really didn't pay too much attention to these e-mails. This whole -- this whole thing is about five minutes of my career, these two e-mails, if that.

There was no follow-up afterwards and there was no real attention to it beforehand. Bottom line is that I skimmed the filings and I missed the write-off

and I made a mistake and sent these e-mails out at the request of my superior.

So -- so to answer your question, at the time, not really being all this focused on this big e-mail and the content within the

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e-mail, I didn't give it a second thought of why I should or shouldn't send it to this list. I simply was asked to send the e-mail out and, unfortunately, because I didn't focus in on the write-down in the filings, I inadvertently sent it out at the request of my superiors.

That is about the extent of this whole e-mail. I feel horrible that I made the mistake. I feel bad that the gentleman lost 15,000 that put it in in December. I am grateful the other guy did not invest. But the fact of the matter is -- and I am embarrassed that I missed it after all this time on Wall Street that I missed it.

I welcome the opportunity to explain the situations that started in July with this whole write-down because there is a reason why I missed it, and that is all this was was an inadvertent mistake on a write-down of an asset that wasn't emphasized by the company.

Q. So is it fair to say you didn't have any congratulatory party following the issuance of these e-mails?

MR. JANGHORBANI: Leading.

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A. Congratulatory party?

MR. JANGHORBANI: There is an objection standing.

JUDGE FOELAK: I didn't actually hear Mr. Hantman's question. I heard the word "congratulatory" but that was about it.

MR. JANGHORBANI: I guess the court reporter can read it back if your Honor would like.

(Record read.)

A. No. There wasn't a party, if I am allowed to answer that.

Q. As you sit here today, are you sorry that these e-mails went out?

A. Absolutely. I have no history of this.

Q. Have you ever indicated to somebody that you are proud that you sent these out?

A. This e-mail was -- was erased from my memory two seconds after I sent it. I didn't really think about it one way or another. Unfortunately, I hit the send button and it's caused me a lot of grief.

But, you know, I mean I made a mistake

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and I am willing to admit the mistake but there is a good reason why I made this mistake.

Q. Well, I don't want to put words in your mouth so perhaps if you can explain the circumstances leading up to the October 1st -- to the October e-mails in

regards to W2E, Charles Vista and the debenture offering?

A. I welcome the opportunity.

Q. Well, that is not what I am asking you --

A. Yes, I would -- can I explain?

Q. Yes, of course.

A. So, Craig Brown and Waste2Energy originally met their accountants in July and in July is when the asset was beginning to be impaired. That is the event, that is the material event.

MR. JANGHORBANI: Your Honor, I am going to move to strike this. There is no foundation for him to know any of that. He hasn't testified that he met with anybody --

JUDGE FOELAK: Okay. Counsel, he is explaining his mental reasoning process, which may have been based on false assumptions but

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that is what I understand he is doing.

THE WITNESS: Thank you.

MR. HANTMAN: Exactly.

MR. JANGHORBANI: But he hasn't laid a foundation for that, your Honor. He hasn't said he spoke to anyone or anyone told them anything.

THE WITNESS: Let me finish, please.

JUDGE FOELAK: Please continue.

THE WITNESS: Waste2Energy, although it is not a piece of evidence, it is not admitted at evidence their investment banking agreement says they would report immediately to Charles Vista when they become aware -- when they become aware of any potential financial change.

And also, they became aware of a potential write-down of 95 percent of their assets in July.

Q. How do you know that?

A. Because Craig Brown said it yesterday.

Q. Okay.

A. In July. Okay?

Q. Go on.

A. Now, the material disclosure is in

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July, when they became aware of the potential write-down of their entire asset base, not in October, number one.

Number two, in order to protect the investment they were still taking money from short-term notes knowing full well that 95 percent of their asset has been compromised and they did not amend their offering documents to reflect that material event. They did not voluntarily disclose it to their investors, and they took money in July, August and September without disclosing a potential write-down.

Number two, they immediately, the second they found out that there was a potential write-down from

their auditors they should have sent an e-mail to Charles Vista calling an emergency meeting to discuss the implications of 95 percent of their asset base being obliterated. They did none of that. None.

There is no documented e-mails or presentations or formal disclosures that this company may have lost 95 percent of their asset base. In fact, the first time they disclosed it was in October. Okay? Yet they continued to

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take countless of hundreds of thousands dollars in July, August and September without disclosing a potential write-down of their asset base number one.

Number two, the reason why I missed this asset is because this needed to be emphasized, emphasized, not minimized and not hidden in a regulatory document. There is no disclosures anywhere, anywhere that this asset may have been written off to 95 percent. None. Zero.

JUDGE FOELAK: Let me just gain a – okay. So sort of to summarize what you have testified is you did not know about the write-down until October and it was, in your mind, hidden somewhere, the disclosure, when it was made?

THE WITNESS: That is accurate. And lastly, the reason why I missed it and it was an unintentional mistake, which is the end of my little spiel, is I didn't -- my mistake is I didn't scrutinize the filings because I did not -- I wasn't led to believe that there were any dramatic changes in these filings.

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And it is my mistake, okay? I thought that if the company was going to write down 95 percent of the assets, that we would have known about it long before the October 1st filing.

The CFO of this company and the other people were experienced guys. They know that these debentures were relied upon this asset base. They knew the importance of this write-down and yet they did not voluntarily disclose it anywhere.

And this deserves more than a phone call. I don't recall any phone calls. And this deserved a Sermon on the Mount meeting to disclose not only their existing noteholders, not only the people that were thinking about buying stock from the marketplace. That is why the 8-K came out, the people that had to buy stock from the street.

Most importantly, they needed to amend their PPM to take on the notes that they were raising money in July, August and September. Think about it. If I invested in July or August I had no idea that this asset was going to be

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compromised. None. And yet I am the guy sitting here on two e-mails. Meanwhile, a whole bunch of Americans and other investing public invested a ton of money into Waste Energy without full disclosure of a potential write-down.

JUDGE FOELAK: Again to summarize, the disclosure in your mind was not illuminated enough?

THE WITNESS: Absolutely. And furthermore, it was not disclosed when it should have been disclosed. Needed to be disclosed when they became aware of it in July, not when -- when they disclosed it, it was too late. It was after the fact. A whole bunch of people already invested.

And that's why I missed the e-mail. I am man enough to say -- I am not going to sit here and say I didn't make a mistake. I made the mistake, I sent the e-mails. I shouldn't have sent them out.

If I scrutinized that filing because it was highlighted and brought to my attention like it should have been -- 95 percent of the

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company's asset base is gone. It should have been discussed. It shouldn't have been just stuck in an e-mail, "Well, hopefully you will catch it." It should have been highlighted, emphasized and discussed on behalf of the investors.

Now, it is my mistake. I missed it. I didn't scrutinize it. This was an unintentional miscue. Now I am paying the price for that mistake. But if anyone says that I maliciously, intentionally, premeditatively sent out e-mails with the intent to defraud, that is a complete falsehood. There is no getting around that statement.

I apologize I sent the e-mail out. It was wrong. I am embarrassed that I missed it. But intentionally defraud anybody? Absolutely not.

Q. I notice Mr. Benkovsky's name is here as a noteholder. Do you know who that is?

A. Stevie B.

Q. That is what he was referred to as?

A. Yes.

Q. Was he a client of Charles Vista?

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A. Yes.

Q. Were you familiar with his $2 million investment?

A. Absolutely.

Q. Do you know when he made this investment?

A. I believe the actual wire was sent to escrow the end of August, maybe early September, give or take.

Q. Do you know whether W2Energy ever notified him at that time in August that they had already been working on working papers to write off this $11 million asset?

A. I don't believe they disclosed it to anybody prior to October 1st.

Q. You heard Mr. -- I think Mr. Brown's testimony. Were you ever aware that the money that was being raised by Charles Vista was going to be used by W2Energy not to enhance the business but to pay off previous bills?

MR. JANGHORBANI: He is leading again, your Honor.

MR. HANTMAN: Okay.

Q. Were you present when Mr. Brown

[p.375]

testified that certain monies were used to pay off accountants? Yes or no?

A. Yes, I was here.

Q. Were you here when Mr. Brown testified monies were used to pay lawyers?

A. Absolutely.

Q. Were you here when Mr. Brown testified that money was used to pay auditors?

A. Correct. I was here.

Q. When Charles Vista took Mr. Benkovsky's money, did you have any knowledge of how W2Energy was going to use his money?

A. My knowledge is that they were going to repay angry noteholders. Angry ones that were in default.

Q. That was your understanding?

A. As well as some back salaries, professional fees and -- if memory serves me -- I could be wrong but I think -- I think a piece of Mr. Benkovsky's money was going to engineering specs on one of their letters of intent. But that may not have been Steve's money. That may have been the prior money.

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But Peter Bohan talked about that they needed a good faith deposit for engineering in order to begin the engineering of some of these units.

Q. Now, can you explain the subscription investing process in the W2E debentures?

A. Sure. In order to subscribe to a private placement at Charles Vista the investor had to be first deemed to be accredited before they even received any information, and they also needed -- you couldn't have a new account to purchase private placements.

So the registered rep -- the registered representative would have to ask a questionnaire, a Regulation D questionnaire and then get that reviewed by Michael Molinaro in order for -- and filed properly for FINRA in order to determine that the investor was accredited and suitable for the investment.

And then once Mr. Molinaro reviewed it and approved it, then the broker would then send subscription documents and offering documents to the investor, which were numbered.

And then the investor would then, you

[p.377]

know, have the opportunity to ask questions and -- to the registered rep and then would have to fill out the purchasing questionnaire and the subscription documents further attesting that they are accredited.

Q. Now, do you know whether this was done by either of the two people who received e-mails from you?

A. From me?

Q. Yes.

A. I didn't do any of this for them.

Q. And in the e-mails to both these individuals it says, "Please read the offering memorandum including all risk factors." Do you know if they even had the offering memorandum?

A. No. I wouldn't know.

Q. Did you ever send them the offering memorandum?

A. No, I didn't.

Q. Subsequently, do you know if anybody ever sent them an offering memorandum?

A. Well, based on the information that I know now it is obvious that the guy who put in – Goolcharan, the guy that invested in

[p.378]

December, by default, had to receive an offering memorandum from somebody.

Q. Did you send it to him?

A. No.

Q. Do you know who did?

A. His broker.

Q. Do you know who?

A. I think it was Gregg Lorenzo. Could have been Adam. I don't recall.

Q. Did you ever solicit Waste2Energy debentures to investors?

A. No.

Q. And why not?

A. I wasn't very good at it, first of all. And second of all, it wasn't the role of a broker. I didn't get on the phone -- I didn't have any retail clients, I managed no accounts, never received any commissions, nor was I a joint rep on any of the investors -- on any client of Charles Vista.

Q. So then were these two e-mails part of like a new endeavor by you to go after retail clients?

A. No. They were Adam and Gregg's

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clients. They weren't my clients.

Q. Was this something you had studied for, how to solicit people through e-mails? Is this something that you studied for?

A. No. No.

Q. Did you ever prepare any Regulation D questions for any deals at Charles Vista?

A. No. That was a function of compliance.

Q. Now, are you the registered representative for any accounts at Charles Vista?

A. No, I wasn't.

Q. Were there people at Charles Vista who were registered?

A. Yes. The brokers.

Q. How many brokers were there at Charles Vista at that time?

A. It varied. Anywhere from 15 to 25 or maybe 10 to 25 over the 9 or 10 or 11 months I was there.

Q. How many?

A. Between 10 and 25 I think would be a good estimate.

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Q. Well, on October 14, 2009, how many brokers worked at Charles Vista?

A. I don't recall exactly.

Q. On the day in question, were there brokers in the office on that day?

A. Yes.

Q. Do you know why you, out of all the people -- you are not a registered representative for any of these people, you are not involved in retail sales, that is not your background.

Do you know why you were chosen or asked by Mr. Lorenzo to send out these e-mails?

MR. JANGHORBANI: Objection. One, leading. Two, lacks foundation. He doesn't know what is in

Gregg Lorenzo's head and he already testified he didn't have any conversations about this e-mail.

JUDGE FOELAK: He did testify he had no conversations. I mean I suppose he could state what his opinion was.

Q. Well, you had no conversation but you were told to -- well, did you send this out on your own? Did you wake up and decide "I am

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going to send this to two people I don't know, have never met and have nothing to do with"?

MR. JANGHORBANI: Objection. Leading.

A. No.

JUDGE FOELAK: Your objection is sustained.

Q. So you sent this out because Gregg Lorenzo told you to send it out but you had no discussions over the substance of what you were sending out?

MR. JANGHORBANI: Objection. Leading.

JUDGE FOELAK: Sustained.

Q. What did Gregg Lorenzo exactly tell to you do?

A. He told me to send --

MR. JANGHORBANI: Objection. Foundation.

Q. Over here it says, "Dear sir: At the request of Gregg Lorenzo." What did you mean by that?

A. Gregg Lorenzo asked me to send that out.

Q. What did he say to you?

A. "Frank, I want this come from our

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investment banking division. Can you send this out for me?" Something like that.

Q. What, if anything, did you say to him?

A. "Sure." The guy owns the firm. He just asked me to send out an e-mail for him. I am going to tell him no?

Q. Did you ask him why?

A. He said -- he asked that -- he said, "I want this to come from the investment banking division."

Q. Was that customary, that the banking division --

A. No.

Q. -- would send out this type of e-mail?

A. No.

Q. Did you find it unusual?

A. Well, in hindsight I find the whole thing unusual, but at the time, you know, at the risk of sounding redundant, this whole thing took about 15 seconds of my day at the time.

So, you know, if I knew that this was going to be -- forgive me for laughing. I don't want to minimize the severity of this, but if I knew that this was going to be the repercussions

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of sending out these e-mails, I would have -- you know, I would have paid attention, I would have questioned, I would have done a whole bunch of things. And at the end of it all, I wouldn't have sent it.

Q. Now, in October of 2009, can you describe the atmosphere at Charles Vista?

A. Yeah. It was a very typical -- for lack of a better word I will use the word "boiler room." It was a small boiler room. You know, a bunch of young guys standing up overcoming objections and pitching stock.

You know, there was -- you know, I have seen this. Over the years I have seen this, you know, young guys fighting and arguing and, you know, and yelling and screaming. I shut my door most of the time but that was kind of the atmosphere of Charles Vista.

The confrontational issues I had at Charles Vista was mostly between Peter Bohan and Gregg Lorenzo, which was whenever there was an escrow close Gregg wanted -- Waste2Energy would end up with 70 percent, 70 percent of every dollar. 12 percent went into a sinking fund,

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18 percent went into for fees, brokerage fees. That was 70¢ of every dollar went to Waste2Energy. And there was always -- there was always tension and yelling and screaming on what to do with the 70¢.

Peter Bohan needed it to fund operations of the company properly and Gregg Lorenzo needed it to repay angry noteholders whose notes are in default.

So I spent a lot of my time playing referee between Gregg Lorenzo and Peter Bohan.

Q. You mentioned there were a lot of young guys who were out there trying to raise money for different -- for Charles Vista. Were you one of those young guys?

A. No.

Q. Can you describe your physical health in or about October 2009?

A. Well, I started having health problems when I worked at John Thomas Financial because --

Q. I am sorry. October 14th, to be more exact. Can you describe your mental condition, physical condition at that time?

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A. Well, mentally and physically in October? Well, you know, I had two surgeries and a blood clot late 2008, early 2009 which -- you know, because of my shoulder and knee surgery I was under -- I had pain medication and I had a blood thinner at the time. So, you know, that was -- I wasn't doing bad health-wise but I wasn't a hundred percent either.

Q. Are you married or you are single?

A. I am single.

Q. Do you have any dependents, anybody you support?

A. My mom. My mom is a widow.

Q. How old is she?

A. 78. Now she is 78.

Q. And you take care of her?

A. Yes, me and my three other brothers and sisters. We financially help mom out.

Just if I may -- you know, towards October, you know, it is -- I was kind of losing Sera. Sera wanted to leave. She wasn't happy. And financially this wasn't working out for me. At that time, even though I didn't leave in October or November, you know, it was that time

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when I started, you know, looking around for a different place to work.

Q. Now, with some of the people who had invested in W2E, did you ever do anything to try to get them to help recover any money?

A. Yeah. There was a lot of -- after I left Charles Vista there was a lot of clients, they didn't want to speak to Gregg anymore, so he would toss them to me after they made their money or the company couldn't repay their defaulted notes and they just didn't want to speak to him anymore. So he would ask me to speak to them.

And, you know, I would tell them, "The company doesn't have the money to repay you." Anyhow, the point being that I started having some dialogue and relationships with these guys, probably about 15 to 20 Waste2Energy investors, both in the equity and the debenture round.

And there was one guy, Steve Pesci from Elizabeth Truck Center, who him and his friend were some of the biggest investors in Waste2Energy. I think they put in, you know, close to a million dollars of the $6 million

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that they did in Mercer.

So anyhow, he was upset and he felt -- he felt taken advantage of so he asked me, "Frank, how can me and my people try and get my money back?"

This happened in -- after the -- after the Waste2Energy was put into involuntary bankruptcy in March or February of 2013 -- or '12. Anyhow, the e-mails say. I think it was '12.

At any rate, I mentioned to Steve, I said, "Steve, look --" I got to know a few of these debentures holders, about 15. "My suggestion is this, you form a group and you try and get some relief as a group from either Waste2Energy or Charles Vista."

I did this – I didn't charge him money to help. I just made the introduction. Steve Pesci then agreed to organize and lead the group. It was maybe 15, 20 from people I referred him to, plus 10. So it turned out to be anywhere from 25 to 30 investors that lost their money. I made the introductions between the

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investor and Steve Pesci that they were both Waste2Energy shareholders and they both suffered losses and I would suggest that you coordinate a group so you can come together in unison to seek any

remedies or collect or so you can get some of your money back.

Q. Was this part of your responsibilities, official responsibilities or duties at Charles Vista?

A. No. I did this after Charles Vista.

Q. At the time that you did that, was that in anticipation that you, yourself, were going to be a target of the SEC?

MR. JANGHORBANI: Objection. Leading.

JUDGE FOELAK: That is –

Q. What was your motive for helping the investors to try to get back their money?

A. Well, believe it or not, I felt bad that they lost all their money, okay? They lost their money. You know, like my testimony said, this was a high risk investment and after getting to speak to some of these investors they weren't disclosed how risky this investment was. This belonged in the risk-oriented

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side of investors' portfolio. If a guy has -- out of 100 percent he should be putting 2 and a half to 5 percent of his investment capital into these deals. These brokers were putting 70, 80 percent of the guy's investment capital into Waste2Energy.

Then when I would talk to the guys, one guy was talked into liquidating his retirement account. One guy was talked into getting -- taking a loan against his business in order to invest in Waste2Energy debentures. One guy took a mortgage on his house

because he was guaranteed or he was led to believe that he was going to be repaid by one of these young brokers.

So here, I get these guys on the phone. One guy almost lost his wife. One guy had to mortgage his house in order to repay the business loan. The other guy blew his retirement account. And I am hearing what they were told. So naturally, here comes -- naturally, you know, despite what anyone may think, I actually felt bad for these guys. I figured it was a long shot for them to try to

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recoup any of their money because, you know, Charles Vista didn't have any money and Waste2Energy was in bankruptcy.

So although it was a long shot, I didn't feel confident -- and I told them, "This is a long shot in order to get money from Waste2Energy."

Q. Do you know why these people called you?

A. I called them. Well, I originally started relationships with them because they got sick of talking with Gregg Lorenzo so they found -- Mike Robbins, Steve Pesci, Dan Casey, a whole slew of them. Marvin Givetts. All these big investors in Waste2Energy.

Because they kept on -- because they didn't want to talk to Gregg anymore, they had to talk to somebody. I talked to them.

Q. But you weren't the registered representative for these people, were you?

A. No.

Q. They were talking to you because they got tired of hearing Gregg Lorenzo's fake information, for lack of a better word?

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MR. JANGHORBANI: Objection, your Honor. Lack of foundation. In fact, I move to strike his last response. He is testifying about other people's motivations. He hasn't laid any foundation for how he knows that.

JUDGE FOELAK: Yes. Sustained.

Q. Did anyone you speak to ever indicate to you why they were calling you?

A. Yes.

Q. What did they say?

MR. JANGHORBANI: Objection. It is hearsay.

JUDGE FOELAK: Wait a minute. You can answer. He is going to explain his understanding of why they were calling him and not somebody else.

A. They were calling because their defaulted notes weren't getting repaid like they were led to believe and they no longer trusted what was coming out of the broker's mouth.

Q. But they trusted you?

MR. JANGHORBANI: Objection. Objection.

Q. Did they indicate they trusted you?

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MR. JANGHORBANI: Objection. It is hearsay. He is putting this in for the truth of the fact that other people trusted him. It is classic hearsay. If he wants to call one of these people he could have done that when his witness list was due.

JUDGE FOELAK: Of course, hearsay is not forbidden in our proceedings. But I guess you are asking for his understanding of their motivation, not really knowing what the motivation really might have been.

Q. What was your understanding as to why they called you, on what facts?

A. To get -- to find out if their notes were going to get repaid and what...

Q. The government's exhibit Division Exhibit Number 19 --

JUDGE FOELAK: Which is in evidence?

MR. HANTMAN: Yes.

Q. How much time, if any, did you spend studying this?

MR. JANGHORBANI: Objection. Leading.

MR. HANTMAN: I am asking how much time, if any, he spent is not leading.

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MR. JANGHORBANI: How much time he spent "studying this."

JUDGE FOELAK: Objection overruled. You can answer.

A. I didn't study it. This was all...

Q. Did anybody call you with respect to the subject matter of this document?

A. I don't recall. I just don't recall having any -- any real conversations about the content of this with anybody. I mean, we may have -- you know, now that I have seen it a million times, my point of view is a little different. At the time -- I mean -- there is just no way that I read this and understood the implications and then would send out an e-mail to those two investors.

So, you know, I probably overlooked it. I just don't see how I...

Q. Did you attend any meetings with respect to the subject matter of this document?

A. No, there were no meetings on it.

Q. Do you have any memos in your file from anybody with respect to the substance of this document?

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MR. JANGHORBANI: Objection. Foundation. He has testified that he didn't talk about it to anyone and didn't attend any meetings.

JUDGE FOELAK: Your objection is sustained. And this e-mail is pretty summary. You don't have to dig down deeply into many, many pages to find out the crucial information about the 11 million.

Q. So you had no follow-up conversations on this?

A. None that I can recall.

Q. On Division Exhibit Number 30, were there any meetings in which the subject matter of this e-mail was discussed?

A. Any meetings on the subject matter of this? There was conversation of the company trying to get a dual listing in Frankfurt briefly in case they never received a relisting but they said they didn't have the money to apply in Frankfurt. But this was briefly addressed. The delisting talked about on the back page was addressed. Not on the page that is up here but the back page.

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Q. In October 2009, did you ever have any argument with Mr. Lorenzo, Gregg Lorenzo?

A. We had arguments at least once a day.

Q. What were these arguments over?

A. Well, I told him that this is not -- that this -- I don't know exactly what I said but what I did tell him is it is just a matter how long the fuse was lit before this bomb goes off. You have debentures going into default while you are raising additional money and taking on additional notes.

It didn't set out as a convertible debt spiral but it has the same implications of a toxic convertible debt spiral. I told him, you are not raising enough money fast enough in order to alleviate debt and grow the company properly. This will explode.

I say it in here somewhere, this needs to be fixed. It needs to be fixed. It wasn't met with any -- it just wasn't taken seriously.

There was also another conversation which caused big, big problems, is I told him -- I suggested that you count how many accredited investors that the firm had. Okay? It came out

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to over 500. I said, "Rather than try to get ten people to put a million or 2 million into Waste2Energy you should recommend a 10 to $20,000 investment to the 500 people in case the deal goes bad you are not causing huge-- you are not hurting somebody."

But whenever I made suggestions to Gregg on how to raise money, you know, it was just never -- it wasn't well received.

MR. HANTMAN: Just a couple more questions.

JUDGE FOELAK: Okay.

MR. HANTMAN: Your Honor, may I take a five-minute recess?

JUDGE FOELAK: Okay. You want ten minutes?

MR. HANTMAN: Yes, your Honor.

JUDGE FOELAK: Very good.

(Recess.)

Q. Mr. Lorenzo, was it ever your intent when you sent these two e-mails out in question here, was it your

intent to deceive these two people who you never met and never knew?

A. No.

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Q. At the time you sent these e-mails out and you weren't a registered representative for these people, this was not even in the scope of your responsibilities --

MR. JANGHORBANI: Leading.

JUDGE FOELAK: Sustained.

MR. HANTMAN: I am just relying on what he testified. I can take what is part of the record --

JUDGE FOELAK: Okay, okay. It is true he testified that he was not the registered representative of these people or apparently of any people.

Q. You testified you didn't know these people.

A. That's right.

Q. You testified you had never spoken to these people?

A. Correct.

Q. You testified you never followed up with these people?

A. Correct.

Q. Was it your purpose to manipulate these people?

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MR. JANGHORBANI: Objection.

Q. Was it your purpose to manipulate them?

A. No.

Q. Was it your intent to defraud these people?

A. No.

Q. It appears that aside from Mr. Brown, the major witness against you for the government is you?

MR. JANGHORBANI: Objection. Leading. Maybe just editorializing.

JUDGE FOELAK: Basically, there is two witnesses – well, three witnesses.

Q. So aside from – well, the gist of the government's case against you is based upon essentially you?

MR. JANGHORBANI: Argumentative, your Honor. It is just argument.

MR. HANTMAN: That is the fact of the case.

Q. It is you –

JUDGE FOELAK: But it is not really something – I mean it is quite obvious that

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there were three witnesses and one was Mr. Brown and one was Mr. Lorenzo, who –

MR. HANTMAN: Okay.

Q. To the extent that the government is relying upon your testimony to find you responsible, did they prepare you for your testimony before this Court?

MR. JANGHORBANI: I would move to strike the first half of the question. It is just argument.

JUDGE FOELAK: Yes. The question is -- well, I mean that is ridiculous. They wouldn't prepare a respondent.

MR. HANTMAN: I think it is ridiculous but he is their main witness.

JUDGE FOELAK: It is a civil proceeding. You are allowed to call them.

THE WITNESS: It is obvious I am the main witness; yes.

MR. HANTMAN: I have no other questions, your Honor.

Oh, just one other question, if you would bear with me.

Q. Do you have any like secondary jobs

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other than working for Hunter Wise -- actually, with Hunter Wise, what do you exactly do with them at this point?

A. Find corporate -- corporate clients that need accredited financing institutionally or private equity clients or public companies that are listed and trading and operating on exchanges that need financing, or M and A clients or any buy side and sell side private companies that are looking to get bought out by the equity groups.

Q. In that capacity, how would you describe your job at the present time?

A. Well, I am working on a company, a public company that is doing $70 million in revenue, that is fully reporting, showing an 8 percent profit margin. I am a selected dealer. There is two other investment banks involved. The company has been public since 2007.

I am working on a Silicon Valley company doing 13 million in revenue called Tradescape that is looking for 4 million in private equity and I am beginning to start a

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real estate investment company with some private equity and hedge fund managers. So the investment is collateralized with the property.

Q. Do you have any source of income other than in the investment banking field?

A. No.

Q. Should the Court find by a preponderance of the evidence that you defrauded or manipulated these two individuals, do you have any other source to make any real money?

A. No. It would be tragically life-altering. I have been doing this -- this is the only career I have had.

Q. You understand the seriousness of what you are being charged with, do you not?

A. Absolutely.

Q. And you understand that depending on the discretion of the Court, naturally based upon the admissible evidence and the elements of proof, that the judge could disbar you for a period of time. Do you understand that?

MR. JANGHORBANI: Objection. Relevance.

MR. HANTMAN: I think this is

[p.402]

relevant.

JUDGE FOELAK: I think he is trying to bring out the effect of a bar from the securities industry on his future income.

MR. HANTMAN: Even more so, your Honor.

Q. At the time that these two e-mails were sent out, were you aware at that time that if you violated certain security laws, particularly the ones you are accused of, that you could lose your livelihood, that you could have no money?

A. Of course I was aware of that. If you violate securities laws you can get disbarred.

Q. Did the thought ever occur to you that you would end up in the situation you are in now?

A. Absolutely not.

MR. HANTMAN: Thank you, your Honor.

JUDGE FOELAK: Okay.

REDIRECT/CROSS EXAMINATION

BY MR. JANGHORBANI:

Q. Now, Mr. Lorenzo, you testified that -- well, withdrawn.

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You testified that Gregg Lorenzo told you that he wanted you to send the deal points e-mail because he wanted it to come from the investment banking division. Do you recall?

A. That sounds familiar. Yes.

Q. Just a couple minutes ago you testified to that; right?

A. Yes.

Q. And you were the director of investment banking. Right?

A. That is correct.

Q. So you understood that Gregg Lorenzo was asking this to go out from your Division. Correct?

A. Yes.

Q. So it was your reputation on the line. Correct?

A. Yes, it was.

Q. And you understood that; correct?

A. Well, I understand it now.

Q. You didn't understand it at the time? When Mr. Gregg Lorenzo told you, "I want this to come from the

investment banking division" that he was saying this is your reputation this

[p.404]

e-mail is coming out under? You didn't understand that?

A. Like I mentioned in the past, I spent about ten minutes on this whole e-mail if that.

Q. So you didn't give it any thought at all?

A. No, unfortunately.

Q. Sent out an e-mail, didn't give it any thought at all?

A. Correct.

Q. You told Mr. Hantman, correct, that you worked at a boiler room. Right? Charles Vista was a boiler room? You just said that?

A. I said that -- I don't know if I called Charles Vista a boiler room but I said, for lack of a better word, I would call it a boiler room.

Q. So you knew you worked at a boiler room and you said that at least one investor sold their home to invest in Waste2Energy debentures?

A. I think one investor sold a mutual fund, one investor took a mortgage, a second mortgage out on their home. Another investor

[p.405]

took a line of credit.

Q. And one investor liquidated their retirement account to invest in debentures. Correct?

A. Correct.

Q. And you argued every day with Gregg Lorenzo. Correct?

A. Yes, I'd say that's correct, yes.

Q. So you said you started looking for a new job in October or November of 2009. Correct?

A. Correct.

Q. Because you wanted to leave. Correct?

A. Correct.

Q. Because you were unhappy at Charles Vista. Correct?

A. Yes. I was unhappy.

Q. You didn't tell the SEC any of this stuff, though, when you testified on November 12, 2009, did you?

A. November 12, 2009? I don't know if it was asked.

Q. Didn't tell it to the SEC, though, did you?

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A. Well, why would I when I wasn't asked?

Q. Why would you tell them the truth; right?

MR. HANTMAN: Your Honor, that is --

MR. JANGHORBANI: Withdrawn.

JUDGE FOELAK: Okay.

Q. Now, the private placement memorandum, Waste2Energy private placement memorandum, that disclosed that the debentures were a risky investment. Right?

A. Correct.

Q. But your deal points e-mail, that says "Don't worry about the risk, you are protected in these other three ways." Right? Is that what you were saying?

MR. HANTMAN: Your Honor, I think it has been asked and answered.

A. I also said refer to the risk factors.

Q. Okay. You said -- I apologize. I am going to mispronounce the name. Steve Pesky?

A. Pesci.

Q. That Steve Pesci worked with some other investors to try and get their money back. Is that right?

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A. Yes.

Q. In 2010?

A. I don't think it was 2010.

Q. When was it?

A. It is on my -- one of the exhibits. I think it is 2012.

Q. It was after you left Charles Vista. Correct?

A. Yes, correct.

Q. All right.

A. After the bankruptcy.

Q. And you said that you helped Mr. Pesci in some way. Correct?

A. I introduced him to other debentures holders.

Q. All right. But this was all after you left Charles Vista?

A. After. Yes.

Q. So after you stood to make any money from Waste2Energy investments. Right?

A. After I stood --

Q. You weren't getting paid on Waste Energy anymore, were you?

A. No.

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Q. You had no reason to help Charles Vista anymore; right?

A. I had no reason to help? No.

Q. In fact, you had no reason to help Waste2Energy once you weren't getting paid by Charles Vista anymore. Right?

A. No. But I did want to help the investor.

MR. JANGHORBANI: Mr. Chan, can you pull up Division 30? That is in evidence, your Honor.

Q. Do you see this is the e-mail chain between you and Mr. Brown, August 19, 2009?

A. Yes, I do.

Q. You got this e-mail; right?

A. Yes, I did.

Q. You didn't miss this one; right?

A. No, I didn't.

Q. In fact, you responded --

A. Yes.

Q. -- to Mr. Brown?

A. Yes.

Q. "Thanks for the update"?

A. Yes, I see that.

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Q. So you read and understood this e-mail. Correct?

A. Correct.

Q. Thank you.

MR. JANGHORBANI: Mr. Chan, can you bring up Division 65, please?

Q. Mr. Hantman asked you some questions about this document. Right? You remember that?

A. Yes, I do.

Q. You are not copied on this e-mail; right?

A. No, I am not.

Q. You didn't write it or send it?

A. No, I didn't.

Q. You never received it. Right?

A. No, never received it.

MR. JANGHORBANI: Mr. Chan, can you turn to the second page?

Q. Do you see there is a column, third column, that says "Note date."

A. Yes.

Q. No dates before October 1, 2009 in that column, are there?

A. That is just an issue date on the

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note.

Q. There is no dates before October 2009 on that column, are there?

A. Yes, that's correct.

Q. Thank you. You can set that document aside.

MR. JANGHORBANI: May I have one second, your Honor?

(Pause.)

MR. JANGHORBANI: I don't have any additional questions, your Honor.

JUDGE FOELAK: Mr. Hantman?

MR. HANTMAN: Just one point.

RECROSS/REDIRECT EXAMINATION

BY MR. HANTMAN:

Q. The government apparently is predicating part of their case on your intent to make money.

MR. JANGHORBANI: Objection, your Honor. He is simply arguing about what our case is at this point.

JUDGE FOELAK: Let's get to the question.

Q. There were questions that you were

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asked about -- that when you helped these debenture holders it was after you were no longer with Charles Vista. Do you recall that question?

A. Yes, I do.

Q. Yes or no?

A. Yes.

Q. And I think another question was you weren't being paid by – you weren't being paid on any transaction with W2E anymore. Right?

A. That is correct.

Q. Assuming the government is correct that whether you got paid or not has an impact on what you do or don't do –

MR. JANGHORBANI: Objection. I am not sure if it is leading or argument. It is not appropriate.

JUDGE FOELAK: Let's leave the assumption out and just get to the question.

Q. Did you, on October 14, 2009, did you have any idea what, if any, money you would earn from Mr. Rothe?

A. 1 percent of the 18 percent was my fee.

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Q. Was that a motive for you to send this e-mail out?

A. I don't think so.

Q. For Mr. -- for Vishal Goolcharan, did you know whether he had money or didn't have money?

A. Well, I -- I know now he was accredited. I don't know his investment profile.

Q. At the time you sent him the e-mail, was it your intent that you were going to make like a fortune off this guy?

A. No.

Q. So did you have any financial incentive on these particular people out of all the hundreds you could have written to, do you have any incentive to send it to these two people to make a buck?

MR. JANGHORBANI: Objection. This is way beyond the scope of my redirect. I will allow it. Go ahead and answer.

A. I made $150. 1 percent of $15,000 from the Goolcharan investment.

Q. Well, were you motivated by the greed

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of money to send these two e-mails out?

A. No.

Q. Were you driven by greed?

MR. JANGHORBANI: Asked and answered.

JUDGE FOELAK: I have guess he's asking sort of globally.

Q. Were you driven by greed?

A. I'd like to think not.

Q. Were you driven by a need to manipulate?

A. I'd like to think not.

Q. Were you driven by a desire to defraud?

A. No.

MR. HANTMAN: Thank you.

MR. JANGHORBANI: Before the Division rests, your Honor, I was –

JUDGE FOELAK: Do you have any further questions for Mr. Lorenzo?

MR. JANGHORBANI: Yes.

MR. HANTMAN: Certainly I have no objection to the government having a full and fair hearing but aren't we like finished now?

JUDGE FOELAK: He seems to be.

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MR. JANGHORBANI: I have a couple more questions.

MR. HANTMAN: I don't think I did that good a job that he has to continue with more questions.

JUDGE FOELAK: You can have another re, re-cross. Not recross. Re, redirect/cross.

MR. JANGHORBANI: Can I have one second, your Honor, just trying to speed this up?

(Pause.)

MR. JANGHORBANI: I don't have any additional questions for this witness, your Honor.

JUDGE FOELAK: Thank you. You may resume your place.

I wanted to make one comment. It is your Exhibit 132. I notice that Social Security number is on it. Before submitting it as an exhibit you should take anything like home address, date of birth or anything like that out and redact it.

MR. JANGHORBANI: We had taken your comment yesterday to be universal so we will

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scrub the exhibits.

Your Honor, we have two exhibits to

* * *

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* * *

JUDGE FOELAK: I would say you should go first. You can mutually agree.

MR. HANTMAN: I think you should go first.

MR. JANGHORBANI: That is fine. It is one o'clock. Maybe we should take a quick lunch break and then have closings if that is acceptable.

JUDGE FOELAK: How long would you like?

MR. HANTMAN: I will defer to the government.

MR. JANGHORBANI: 45 minutes.

JUDGE FOELAK: Sounds good. So quarter of 2.

(Luncheon Recess.)

AFTERNOON SESSION

JUDGE FOELAK: Good afternoon. Mr. Janghorbani?

MR. JANGHORBANI: Thank you, your Honor.

During opening remarks yesterday, your

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Honor, I told the Court there was no genuine dispute, there couldn't be any real dispute that the statements about protection, all of them in Mr. Lorenzo's October

14, 2009 e-mails were false. I also said there is no real dispute, there can't be any real dispute that Mr. Lorenzo knew, knew for a fact that those statements were false before he sent those e-mails.

Now we have heard from Mr. Lorenzo, we have seen all the other evidence in the case and there is still no question about his liability.

Moreover, now that we have heard from Mr. Lorenzo there is no question that he acted with a high degree of scienter and the fact that he continues to refuse to accept an iota of responsibility for his own actions.

Starting with the e-mail, there is no question he sent it. He admits sending it. He admitted yesterday authoring it. He said. "If memory served, I authored it" and that it was approved by others.

It's his e-mail address, he signed it. That's his signature block right there, director of investment banking. There is no question he

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sent it. There is no question each layer was a complete myth.

Mr. Chan, Exhibit 34, please.

And there is no question that he knew. Waste2Energy had nowhere near $10 million in assets on October 14th, confirmed or otherwise. And we know that because it is right there in the company's October 1st amended 8-K and 10-Q. Mr. Lorenzo admits receiving both of those filings and he admits reading them.

He now says, well, I guess I missed this one thing in the filing. I guess I missed that they had written off all their assets. But that is utter nonsense. This is what he had been focused on all summer. We saw him over and over asking Waste2Energy to confirm that these assets still existed.

Now he is saying, well, I guess I missed them because they were buried. But the 10 million write-down, that was on the first page of the audited financials in the 8-K and it was only on the fourth page of the 10-Q.

And just to confirm it, to underline it, Mr. Brown sent him another e-mail on

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October 5th.

That is Exhibit 19, Mr. Chan.

We spent a lot of time looking at this. Once again Mr. Lorenzo has admitted receiving it and reviewing it. Once again he says he missed this, that it was buried. And once again, that is nonsense because it's right there. The first line of point 2. All he had to do was read three lines into this e-mail.

He did read three lines into this e-mail. He knew very, very well that this number had been written off. In fact, Mr. Brown confirmed that when he said he told him by telephone.

So the company didn't try to hide it. They couldn't hide it. It was really the only number that mattered and Mr. Lorenzo knew about it.

Even if he didn't read the 8-K, the 10-Q, and this October 5th e-mail, even if he didn't do that – he did, but even if he didn't it was incredibly reckless, highly reckless for him to send his e-mail without checking that the asset still existed.

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He knew that an audit was going on. Once again, he had been following the progress of the audit. We see that in the e-mail trail. So he knew there was an audit going on, knew the asset number might change. In fact, when he wrote to the company on September 1st he left a blank for what the asset was worth because he knew he didn't know how the company was valuing it. So, it would be extremely reckless for him to send an e-mail saying 10 million in confirmed assets existed without at least checking with the company.

The statement – even if you accept everything Mr. Lorenzo has said, his statement about the $10 million asset is misleading for two other reasons. The two reasons that he knew it was false, that he didn't ever have to read the 8-K for, that he didn't ever have to receive the e-mail from Mr. Brown, because he said that asset was confirmed. He said it provided protection. But he knew all along that wasn't true.

He testified from the stand that he took the 10 million from an old filing, that it

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was unaudited, never been confirmed by an auditor, that it wasn't confirmed by the company, that he knew that. And in fact he had grave concerns about what that asset was worth from the beginning, from March

to April when Waste2Energy became an investment banking client of Charles Vista's.

He said he thought all along the company would never be able to get 10 million for it, that in his mind it was a dead asset, that the company would be lucky to get a million dollars. So he knew it wasn't confirmed, and he knew it provided no protection and he didn't ever have to read the 8-K, the amended 8-K or the 10-Q or Mr. Brown's e-mail to know that, though he did read all of those documents.

He had no business telling anyone that the 10 million existed, that it was confirmed or that it provided any protection. And there is also no question -- 34 again Mr. Chan?

There is no question that his second statement wasn't true, that Waste2Energy did not have $43 million in multiple orders and letters of intent. Mr. Lorenzo knew back in August of

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2009 that the company only had projections, projections that the 43 million was a projection, a non-binding LOI.

Never came to fruition. In fact, Mr. Lorenzo testified that he thought by September that it wasn't going to come to fruition, so he had no business creating the impression that this company had millions in sales and millions in orders let alone creating the impression, just outright saying, as he did, that it protected debentures from default.

The last statement, he says Charles Vista has agreed to raise additional money. He has admitted this

was misleading. It is more than misleading; it is outright false, as we heard from both Mr. Brown and Mr. Lorenzo, because there was no written agreement. There was no agreement between Charles Vista and Waste2Energy to raise additional money and there was no agreement stated in the note. Mr. Lorenzo said that.

In any event it was at a minimum highly misleading. Mr. Lorenzo didn't even believe Charles Vista had the ability to raise

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additional money. And that belief, that was a well held belief.

The company Waste2Energy was highly in debt, needed $4 million just to pay back old noteholders. And Charles Vista had already tapped out their investor base. They had already put 70 percent of the money they managed into Waste2Energy. No reason to think they could find any more.

And Waste2Energy did default on its debt. Mr. Brown told us that too. And Charles Vista didn't raise any money to bail them out as Mr. Lorenzo had promised they would.

So, he knew each of the statements was false when he sent his e-mail. He really can't deny that. Instead, all he says was that he was checked out, that Gregg Lorenzo asked him to send the e-mail, didn't really read it -- despite saying he authored it, he also said he didn't read it so he can't be responsible for his own words.

We know that is not true. One, because he admits authoring it. Two, because Frank Lorenzo admitted under oath in July of

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last year that Gregg Lorenzo never spoke to him about the deal points e-mail, never spoke to him about the subject matter of the deal points e-mail. He also testified that no one ever gave him any false information about the $10 million asset.

So, if no one said anything to him about the e-mail, no one gave him any false information about the asset he couldn't -- he can't say that someone else did this. He did it. He wrote this false information.

We also know he wasn't checked out. We know exactly the opposite was true. The documents show that Mr. Lorenzo was doing his job as director of investment banking, that he was doing it very carefully in summer and fall of 2009. We saw that he kept bugging Waste2Energy to get him the information about the 10 million. "We need to know about this, we need to tell investors about it because that is what is going to sell the securities. What is going on with the asset? Tell me."

We saw this over and over. We know he followed the audit closely. We see e-mails

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about that too. So we know he was doing his job. For him to say he is checked out now is just nonsense. Even if we credit his story, somehow credit he didn't read any of the documents he admitted reading and he

didn't really read the e-mail that he admitted writing -- even if we somehow credit the argument, it doesn't help him.

That is the definition, that is the dictionary definition of recklessness. He closed his eyes to the danger that his statements would mislead investors. Even if you credit everything he has said, minimally he is reckless, and that is sufficient for scienter under Section 10 (b) and Rule 17 (A) (1). 17 (A) (2) and (3) we don't even need to show scienter, just negligence. No question about that.

No one is denying that Gregg Lorenzo is a fraudster. No one is denying he committed fraud. We sued him, and Frank Lorenzo says he knew he was a fraudster. He says as of the summer, the summer of 2009, he understood he was working in a boiler room, that false

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statements -- sorry. That the truth was being stretched, as he said, to clients, to brokerage clients. He knew all of this yet by his own statement he simply accepted an e-mail from Gregg Lorenzo, just accepted it, didn't read it, didn't check it.

Once again, that is reckless. Even if we accept every single thing he said as true, he acted recklessly. And we shouldn't accept it. It's rubbish. He knew for a fact the 10 million asset didn't exist. But even if we accept it, he still acted recklessly.

So he is lying about fundamental aspect of Waste2Energy's business. He said there were millions in assets, millions in orders, lied about fundamental

aspects of the offering. He said essentially it was guaranteed by Charles Vista. "Charles Vista would get you more money to pay you back. Don't worry about it."

He says now he had no reason to do that. First of all, we don't have to prove motive, but he did have a motive. He was hoping to get paid. He says now he only got 1 percent,

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but at the time he was hoping to get between 7 and 9 percent of all the debenture money he raised. He said that from the stand, too. Gregg Lorenzo had promised that.

And Charles Vista, the company he worked at, the company at which he was the director of investment banking and for whom Waste2Energy was essentially their own client, that company was getting 20 percent, nearly 20 percent of all of the money offered in the debenture sales. Charles Vista and Gregg Lorenzo wanted to keep that money coming in. Gregg Lorenzo of course admitted that percentage, that cut was exorbitant, but they wanted to keep it coming in.

Now, were the false statements material? There really can't be any question about that. The 10 million, the truth was that they had less than 4 percent of what Mr. Lorenzo said they had. They had less than 4 percent of 10 million. That is material as a matter of law.

But Mr. Lorenzo has also admitted that it was material. We heard him do that from the

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stand repeatedly. He called it a big deal and a kick in the stomach when the company wrote off the asset. So, we know he thought it was material.

Mr. Brown said it was material, said the write-down was material. And combined with the other so-called layers of protection, what Mr. Lorenzo was doing was he was creating the impression that these debentures, that they were a safe investment because you had multiple layers of protection. If one fell through, you had these other two.

So he took a highly, highly risky bet, a highly risky investment – and he admitted he knew it was highly speculative – and tried to paint the picture it was a sure thing. Of course that is material. Of course that was important.

Now, he has a number of other excuses, the main ones, that he's checked out, we went over that. He's also said that he wasn't soliciting investments. But all you have to do is read the e-mail. That is exactly what it is, a solicitation. He writes, "I am sending you

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this e-mail to tell you, to summarize key points about the offering." He then goes through some of the points, tells you how you are protected and you are not going to lose any money and he says, "Call me with questions." The whole e-mail is a solicitation. That is exactly what he was doing.

Then he also says, "Well, I directed investors to the risk factor section of the PPM. Hey, hey, don't

blame me if I was lying to them here because I said go look over at this other thing, you will figure out how risky it is."

That is of no moment, doesn't make any difference here, doesn't lessen the materiality. One, there is no evidence that the PPM, the private placement memorandum, was ever sent to the investors, to William Rothe or Mr. Goolcharan. At least not to Mr. Rothe. And it doesn't matter because his false statements in the deal points e-mail, they don't contradict anything that is said in the PPM.

The PPM says nothing about the value of the intangible asset. In fact, that is a telling point and he knew that as well. He knew

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that on September 9th the company wasn't giving any value, wasn't saying anything about the value to the investing public. So his statement is not at odds. In fact the 8-K and 10-Q, they discuss the value of the assets as of March and as of June.

He made a misstatement about the assets on October 14th. He doesn't say -- the PPM doesn't say anything about the number of orders, anything about the number of letters of intent, anything about how real those orders may be. It certainly doesn't say anything about Charles Vista's willingness to raise more money. So, they are just not at odds.

But more fundamentally, in a public enforcement action like this one, investors have a right to believe what their broker is telling them. They are

not required to become Sherlock Holmes and sleuth out the truth to figure out if they are being lied to.

It is not a question of whether they relied. It is not a question whether their reliance was justifiable. That is simply not relevant here. The only question is whether the

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false assets would be important to a reasonable investor, and obviously they were. He was saying your investment was safe. He knew that wasn't true.

There is no question about his liability on all counts. And there is really no question about the relief that the Court should impose. The Court should impose third tier penalties. The number of false statements can be arrived at in all number of ways in this case because virtually every statement there under the three layers of protection is false for multiple reasons. Third tier penalties are appropriate, industry bars and cease and desist orders.

His actions were egregious. What he lied about was fundamental to the company and the offering and he knew it. These were fundamental lies. He told them with a high degree of scienter for the same reason. He is still in the industry so he has plenty of important to do it again.

Most critically, your Honor, he refuses to recognize that his actions were

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wrongful. He continues to try to minimize his scienter. When given a chance to come clean he forced the

Division to trial despite the fact that the evidence is overwhelmingly against him. And he has continued to make up excuses at the trial, saying that he didn't pay attention, that he was checked out.

In fact, he had the opportunity to come clean years ago but he chose not to. He was asked by the staff during testimony in November -- on November 12, 2009, less than a month after he sent this e-mail, to explain Charles Vista's business.

Now, this was at a time when he now says he was in constant argument with Gregg Lorenzo, that he understood he worked in a boiler room, that he thought the brokers were stretching the truth with clients, that he wanted to get out. But when asked to explain Charles Vista's business by the staff, under oath, he didn't say any of that stuff. He said he was proud of Charles Vista's work. He said, present tense, at the time, it was a high quality investment bank. And he said that Gregg

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Lorenzo was honest.

So, he could have come clean four years ago but he kept lying. He kept dissembling and he did it to keep working in the industry. So, there is no reason to believe that this won't happen again if he isn't barred.

In sum, your Honor, there is no question about Mr. Lorenzo's liability and there is no reason to believe he regrets anything other than getting caught.

Thank you very much.

MR. HANTMAN: Your Honor, a very thorough presentation, and I would think that is probably the argument made on almost all of these fraud cases. In fact, it could have been the same argument with Sera Holmes. She wrote the exact same e-mail. She is not here today.

It could have been a statement against Michael Molinaro, the government's own exhibit, Division Exhibit 77, which you have in front of you, that is dated October 14, 2009. That is like the same day that the e-mail went out. And Molinaro, who is the compliance officer -- and this is really inexcusable. He sends an e-mail

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to all the brokers -- this is the government's exhibit. He sends something to all these brokers saying this could be sent out to the public, and on page number 4 it has total assets as of June 30, 2009, $14 million.

This is the government's exhibit. Okay? On the same day the chief compliance officer is sending something out, Sera Holmes is sending something out. This is like selective prosecution.

I am not saying that they are wrong to police the industry. They should be praised and lauded for going after people in the industry. The reason they are going after Francis Lorenzo is, unlike Molinaro and probably unlike Holmes, Mr. Lorenzo, they have the advantage of having their primary witness being Mr. Lorenzo. Without Mr. Lorenzo as the witness they would have no case.

They could have conjecture, they could have supposition but they wouldn't have a case. This is like probably one of the only cases in history where the government's case is built almost entirely, entirely on the respondent.

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To put this in the right context, the government gives Mr. Lorenzo much, much too much credit. They are giving him much too much credit because he is described as -- "he knows how to paint the picture." These aren't my words. This is counsel's words. He knows how to paint the picture, conjured up he is some kind of financial fraudster genius.

"He kept dissembling," as if there is some kind -- as if this gentleman -- you heard him testify. You saw him. You will make your own judgment as to his intelligence, his convictions, his integrity. I think he is anything other than some great dissembler of information.

Certainly I don't think he is -- I won't say capable. I think it is clear he is not trying to paint a picture. You talk about -- this was to mislead investors? Well, let's call a spade a spade. Mislead investors? There is two people here. Two people. One who didn't even open this letter; it was in spam. And the other person, we don't know all the details, okay?

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And I am not minimizing that what Lorenzo did I think was negligent. I won't even say negligent. It was inappropriate. It should not have been done. But I don't think for a second it is Mr. Lorenzo's position

from the beginning that he doesn't recognize responsibility, that he doesn't recognize what was done, in hindsight, he would not have done.

How could the government say that? He's the one who testified for them. If he is such a dissembler of information, he is a genius in painting pictures, he is some material fraudster who is misleading investors -- why would he show up -- this is his fourth time. They are not really relying on anything he said on 11/12/2009. There is not really any evidence, any material evidence.

On 12/16/2009 he was interviewed again under oath. I don't think there is any real evidence there the government is relying upon.

On 3/10/2010 again they had the chance, you know, to go at him. And believe me, they are fine lawyers. There is more than one lawyer involved. Sometimes there are two, three

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lawyers there.

We are talking about the fourth time. The fourth time they speak to Mr. Lorenzo, whom they paint a picture which you may apply to certain people on Wall Street but I don't think it applies to Mr. Lorenzo. The fourth time this great dissembler of information, this guys who is not recognizing what he did was wrong, he comes to a hearing without a lawyer.

Is that like a deceptive act? Is that something that somebody who knows he did something wrong is going to go, to a deposition or hearing in front of the

SEC with highly qualified attorneys and not have a lawyer?

To suggest that he thinks he did nothing wrong, that he is not accepting any liability for what he did -- I think the whole government's case is based upon his testimony on July 26th.

So on the one hand they are saying the man lies, he schemes. At the same time they are relying upon what he said during the testimony. And the testimony -- when they said, "Did you send these e-mails?" He could have said, "I

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don't know." "I don't recall." "No."

He told the truth. "Yes, I sent them." Is that the mark of a genius or some guy who has an intent, a scienter to defraud people?

He is asked the question, was this true? Was this true? Was this true? And at this point -- and his testimony speaks for itself. He said some of these things, you know, he didn't think were true.

They asked the question. It wasn't true then, or now? And even the government was a little bit confused as to what he meant. And he said, "I can't say for sure I didn't know then." That is really what he said. Maybe not those exact words but you have the transcript in front of you, it wasn't that he said, "Yes, I knew at the time I sent these it was wrong."

He never said that. He said, "I can't say now that I didn't know then." Okay? So what does the government have? Some ambiguity as to what he knew

then and his motive as to why he did what they say he did.

So what do they do? And I am not criticizing them. They have done, I think, a

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highly effective job at trying to take something which really is a second thought -- if it wasn't for Gregg Lorenzo and Vista, Francis Lorenzo wouldn't even be here. Or Molinaro. He should be here; okay? Or Holmes should be here; okay? But it was because of Gregg Lorenzo that all this time and this money was spent on investigation.

Again, the government is to be applauded. I am not here to apologize on behalf of any of the defendants. But I think in this particular situation when you look at Mr. Lorenzo, I don't think you can look at it in the abstract or in a vacuum. I have every confidence that your Honor, hearing these cases day in and day out, you get a sense of who is sharp and who knows what they are doing and who is consciously defrauding people and trying to make a buck and trying to cover it up and shift responsibility and have high priced lawyers who they can afford to pay because they are making a fortune off the public.

I think this Court certainly has the ability to say to themselves, this guy is like a

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relatively -- I won't say pathetic guy, but he is a guy who got involved with people who are like wolves, who were very cunning and sort of used him and mistreated

him and created a situation where he did something which was stupid.

But I don't think it rises to the level of scienter where he decided on October 14, 2009, "Well, today is a beautiful day. Who can I defraud? Who can I send an e-mail to so I can make a buck today? Oh, I get it. Let me send it to some guy in South America --" wherever the guy is, "-- and let me send it to somebody else. I don't know these people. I am not a registered agent with these people. I have no idea what they know. I am going to pick these two people because this is my goal to get rich. This is my -- I have been waiting my whole life to send two e-mails to two people I don't even know, it is not my job."

Then to suggest that this was some scienter, he had a plan, he knew it was material misrepresentations, he was going to trick these people? Well, if that was his plan, why didn't

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he follow up with another e-mail? I am sure he could have gotten their phone number and called them up. If this was an opportunity to mislead investors and make a big buck, these were not the right people to go after.

Clearly the fact of who he sent this to, who they are and the fact he had little or no contact with these people doesn't lend itself to believe that he had the requisite intent to defraud these people. It is consistent with the fact that Gregg Lorenzo told him to send it out; he sent it out. There is no follow-up, no rhyme, no reason.

Frankly, it is like stupidity. It is laziness maybe. Maybe it is irresponsible. But I don't think -- of course, you will make the final decision. I don't think this particular case raises to that level.

Now let's go a little bit further. I think most people who come before this Court -- it is a very serious Court -- it is usually not like their first time I would think. Maybe once in a while it is a first time, but Gregg Lorenzo, he had a whole history of problems.

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Certainly the government does a thorough job. In all the years that Mr. Francis Lorenzo has been in business, his testimony, other than one FINRA thing which I don't know the details of, no one has ever gone after him. He has never been a target.

Since 2009 -- it is 2013 now. As far as he's out there, he is like lurking, he can do stuff and go after the public again? No one has come forward and said he is doing anybody any ill or defrauding people.

He is making a living, he is not with Charles Vista, he is not with John Thomas. Finally he found a home. He found a legitimate place where he is not doing like retail sales. It seems like he is doing more investment banking. It is not the toxic environment from which he came.

For once he probably found a position which lends itself to his abilities and even his frailties, because around the sharks, he will be eaten up. There is no question. I mean, you talk about sharks? This guy doesn't even have a life preserver. He goes to hearings without any

[p.460]

lawyer. That could really be a plan, that it was his intent, as suggested by the government that during the whole course of this proceeding he's misled people and has not taken responsibility?

I saw the letters he wrote to your Honor. I see some of the communications he had with the government. He is like a pathetic figure who is trying to, you know, hire somebody to represent him without any money.

I think for the government to selectively go through different documents -- they have a hundred some documents here. There is how many? Probably 50 or 60 documents. If this case were so simple and so obvious, so blatant, do you need 60 exhibits? What the government is doing -- and I am not blaming them. Like I said, they have done a thorough job because they prepared to go after Gregg Lorenzo and Charles Vista. He is the money guy, he is the guy with the high-powered, excellent lawyers. They were going to go after him but that resolved itself so that is why we are here.

Should Mr. Francis Lorenzo have maybe

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talked to them sooner? Should he have maybe cooperated, which -- they say he didn't cooperate but obviously he showed up when he was supposed to show up and gave testimony. They like his testimony, or some of his testimony.

Maybe he could or should have done something, but is that a reason to go after him with more of a

vengeance? I would think not. I would think that it shouldn't be held against him that he either had ineffective counsel or not competent counsel or maybe he had great counsel but he didn't keep the counsel, you know?

Or should it be held against him that this case has gone this long or this far? It really didn't go this long or this far because of Francis Lorenzo. It went this long and this far because the government was going after Gregg Lorenzo. And they settled with him just recently. It wasn't a long time ago.

So there is not all this money spent and resources and energy because of this action. This is just like a sideshow. It is an important show. I think when you look at all –

[p.462]

now the explanation for what happened -- I mean, I don't think you can say he doesn't accept responsibility. He was on the stand and he said, "I did this because of this. I didn't spend too much time thinking about it. I was wrong. I wish I had never done it. I made a mistake. I am sorry:

He said that. What does the government want him to do? I don't know what they want. They are arguing that somehow he should be disbarred and there should be three tier penalties and all the cease and desist because he doesn't accept responsibility?

Well, you will make the final decision as to whether this gentleman is arrogant and egotistical or whether he is a person who made a mistake.

The first time he is done anything, that he is even accused of anything at this level. Certainly I would ask that the Court look at the totality of circumstances to see whether in this situation with this particular individual, given the fact that he was -- he is so far removed from these people who he

[p.463]

supposedly made these material misrepresentations to.

If this was part of some scheme or something, why would he limit it to these two? He has a list. There is a list in this book here of hundreds of people who put money into the company. If this was the kind of thing, as the government would have this Court believe, why didn't he just send that e-mail out to Benkovsky and all those people? Those people would have had much more motivation to put more money in at that time if they had gotten this information.

So this is really an aberration. If this was a federal criminal case I think it could be seen as an aberration. It is not consistent with what the respondent does day in and day out.

I can go on and on but really it is not for me to argue with this Court or trying to convince you. You are way more competent than me to come to a conclusion. I am not going to go on and on and on. I think I am just responding to the government's position and I

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would hope, and on behalf of my client, thank you for the time you have taken to hear this case.

We would ask that you ultimately -- I know you are going to want submissions -- but make a finding based upon the facts and the preponderance of the evidence. All of the statements as to what he knew and he did this and did that and did this, I believe, is conjecture. I think the government -- maybe they are right, maybe they are wrong, but I think if it is 50/50 this Court would find that the government has not reached the level which they are required to reach.

Based upon that we'd ask that you come back with the decision consistent with the law and the facts and the reality of the situation.

Thank you, your Honor.

JUDGE FOELAK: Okay. Thank you.

As you reference, post-hearing briefs are appropriate. Has there been any consideration of whether you would file simultaneously or sequentially and what dates?

MR. JANGHORBANI: There hasn't been.

[p.465]

I would propose we file simultaneously end of October, since we are at end of September.

* * *

Div. Ex. 34

From: Francis Lorenzo [Florenzo@charlesvista.com] on behalf of investmentbanking [investmentbanking@charlesvista.com]
Sent: Wednesday, October 14, 2009 3:33 PM
To: vishal.goolcharan@ **Redacted**
Subject: W2E Debenture Deal Points

Dear Sir:

At the request of Adam Spero and Gregg Lorenzo, the Investment Banking division of Charles Vista has summarized several key points of the Waste2Energy Holdings, Inc. Debenture Offering.

******Please read the Offering Memorandum, including all "Risk Factors"******

12-month Note, Debenture pays a 12% interest rate, paid quarterly

A sinking fund has been created, handled by 3rd party (SRFF attorney). Interest payment amount will be held in the sinking fund

This is senior debt. There is no other debt (other than simple debt). These debenture holders have to approve (51%) any other debt.

If there is a liquidation, these debenture holders get paid first.

There are 3 layers of protection:

(I) The Company has over $10 mm in confirmed assets

(II) *The Company has purchase orders and LOI's for over $43 mm in orders*

(III) *Charles Vista has agreed to raise additional monies to repay these Debenture holders (if necessary)*

Debenture Holders have the option to convert their debt at $1.00 into common stock. These shares would hove been already added to the Registration Statement

Debenture Holders will receive a 3-year warrant to purchase shares of the company's stock at $2.00 per share. Debenture Holders will receive this warrant regardless if they convert or not.

Please call with any questions-

Truly,

Francis V. Lorenzo
Vice President - Investment Banking
Charles Vista, LLC.
100 William Street
18th Floor, Suite 1820
New York, NY 10038
Direct: 646.422.3113
Toll Free: 800.799.9070
Main: 212.690.6000

From: Francis Lorenzo [Florenzo@charlesvista.com]
Sent: Wednesday, October 14, 2009 3:37 PM
To: wsrothe@ **Redacted**
Subject: W2E Debenture Deal Points
Attachments: image001.gif

Dear Sir:

At the request of Gregg Lorenzo, the Investment Banking division of Charles Vista has summarized several key points of the Waste2Energy Holdings, Inc. Debenture Offering.

******Please read the Offering Memorandum, including all "Risk Factors"******

12-month Note, Debenture pays a 12% interest rate, paid quarterly

A sinking fund has been created, handled by 3rd party (SRFF attorney). Interest payment amount will be held in the sinking fund

This is senior debt. There is no other debt (other than simple debt). These debenture holders have to approve (51%) any other debt.

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No. 17-1077

In the Supreme Court of the United States

FRANCIS V. LORENZO,

Petitioner,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF FOR PETITIONER

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QUESTION PRESENTED

The antifraud provisions of the federal securities laws prohibit two well-defined categories of misconduct. One category is the use of *fraudulent statements* in connection with the offer and sale of securities. The other category is employing *fraudulent schemes* in connection with the offer and sale of securities. In *Janus Capital Group, Inc. v. First Derivative Traders*, 564 U.S. 135 (2011), this Court considered the elements of a fraudulent statement claim and held that only the "maker" of a fraudulent statement may be held liable for that misstatement under Section 10b(b) of the Securities Exchange Act of 1934 and SEC Rule 10b-5(b).

The question presented is whether the D.C. Circuit erred in concluding a misstatement claim that does not meet the elements set forth in *Janus* can be repackaged and pursued as a fraudulent scheme claim under Section 10(b) of the Exchange Act, Rules 10b-5(a) and (c) and Section 17(a)(1) of the Securities Act.

STATEMENT PURSUANT TO RULE 26.9

Petitioner's corporate disclosure statement was set forth in the Petition for a Writ of Certiorari. There are no amendments to that statement.

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BRIEF FOR PETITIONER

Petitioner Francis Lorenzo respectfully submits that the judgment of the D.C. Circuit upholding the SEC's finding that Petitioner violated Section 10(b) of the Exchange Act, Rules 10b-5(a) and (c) and Section 17(a)(1) of the Securities Act should be reversed.

OPINIONS BELOW

The D.C. Circuit's opinion and Judge Kavanaugh's dissent (Pet. App. 1-50) are reported at 872 F.3d 578 (D.C. Cir. 2017). The opinion and order of the Securities and Exchange Commission ("SEC") (Pet. App. 51-95) are available at Exchange Act Release No. 74836, 111 S.E.C. Docket 1761 (2015 WL 1927763). The relevant initial decision of the SEC administrative law judge (Pet. App. 96-121) is available at 107 S.E.C. Docket 5934 (SEC Initial Decision Release No. 544, 2013 WL 6858820).

JURISDICTION

The judgment of the D.C. Circuit was entered on September 15, 2017. (Pet. App. 1-50). On December 19, 2017, Chief Justice Roberts granted the Petitioner's request to extend the time to file a writ of certiorari to and including January 26, 2018. The petition was filed on January 26, 2018 and granted on June 18, 2018. This Court has jurisdiction under 28 U.S.C. § 1254(1).

STATUTES AND REGULATIONS INVOLVED

Section 17(a)(1) of the Securities Act of 1933, 15 U.S.C. § 77q(a)

Fraudulent interstate transactions

(a) USE OF INTERSTATE COMMERCE FOR PURPOSE OF FRAUD OR DECEIT It shall be unlawful for any person in the offer or sale of any securities (including security-based swaps) or any security-based swap agreement (as defined in section 78c(a)(78) [1] of this title) by the use of any means or instruments of transportation or communication in interstate commerce or by use of the mails, directly or indirectly—

(1) to employ any device, scheme, or artifice to defraud, or

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j

Manipulative and deceptive devices
It shall be unlawful for any person, directly or indirectly, by the use of any means or

instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, or any securities-based swap agreement any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

SEC Rule 10b-5, 17 CFR 240.10b-5

Employment of manipulative and deceptive devices.
It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.

STATEMENT OF THE CASE

The antifraud provisions of the federal securities laws prohibit two well-defined categories of misconduct in connection with the offer and sale of securities. One category is the use of fraudulent statements in connection with the offer and sale of securities; the other category is employing fraudulent schemes. With regard to fraudulent statements, Section 17(a)(2) of the Securities Act of 1933 (the "Securities Act") establishes liability for misstatements and proscribes obtaining money or property by means of any untrue statement or omission of a material fact. Likewise, Section 10(b) of the Securities and Exchange Act of 1934 (the "Exchange Act") and SEC Rule 10b-5(b) thereunder prohibit making any "untrue statement of a material fact. . ."

With regard to fraudulent schemes, Section 17(a)(1) of the Securities Act prohibits anyone from employing any "device, scheme, or artifice to defraud" in the offer or sale of securities. Likewise, Section 10(b) of the Exchange Act and SEC Rule 10b-5(a) prohibit anyone from employing "any device, scheme, or artifice to defraud" in connection with the purchase or sale of securities and Rule 10b-5(c) prohibits anyone from engaging in "any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person. . ." in connection with the purchase or sale of securities. Claims brought under Rules 10b-5(a) and (c) are generally referred to as "scheme liability" claims. *See, e.g., In re DVI, Inc. Sec. Litig.*, 639 F.3d 623, 643 n. 29 (3d Cir. 2011), *abrogated on other*

grounds by Amgen Inc. v. Connecticut Retirement Plans and Trust Funds, 568 U.S. 455 (2013)("We refer to claims under Rule 10b-5(a) and (c) as 'scheme liability claims', because they make deceptive conduct actionable, as opposed to Rule 10b-5(b), which relates to deceptive statements.")

Courts have described Section 17(a)'s proscriptions as "substantially identical" to those in Rule 10b-5. *See, e.g., Landry v. All Am. Assurance Co.*, 688 F.2d 381, 386 (5th Cir. 1982); *SEC v. Monarch Funding Corp.*, 192 F.3d 295, 308 (2d Cir. 1999) ("Essentially the same elements are required under Section 17(a)(1)-(3) in connection with the offer or sale of a security" as under Rule 10b-5, "though no showing of scienter is required . . . under [Section 17](a)(2) or (a)(3)."); *SEC v. First Jersey Sec., Inc.*, 101 F.3d 1450, 1467 (2d Cir. 1996) ("With respect to § 17(a)(1), essentially the same elements [as in a Rule 10b–5 claim] must be established in connection with the offer or sale of a security.").

Here, Petitioner, who was the head of investment banking at a stock brokerage firm, sent an email to two investors that was written by his boss. The email concerned an upcoming bond offering by Waste2Energy Holdings Inc., one of the firm's corporate clients. The email turned out to have three misstatements in it concerning the features of the bond offering. The D.C. Circuit held that Petitioner did not violate Rule 10b-5(b) because he was not the maker of the statements in the email because his boss retained 'ultimate authority' over the statements under the holding in *Janus Capital*, 564 U.S. 135, 142 (2011). (Pet. App. 2). However, the D.C. Circuit held that even though

Petitioner was not the maker of the misstatements he could still be held liable as a primary violator of Rule 10b-5(a) and (c) and Section 17(a)(1) for the same misstatements under a theory of scheme liability because Petitioner helped produce and distribute the two emails.

The D.C. Circuit erred in its holding that Petitioner's ministerial acts in helping produce and send the two emails may constitute the basis for imposing scheme liability. Claims for fraudulent statements are distinct from claims for fraudulent schemes. *Desai v. Deutsche Bank Sec., Ltd.*, 573 F.3d 931, 939 (9th Cir. 2009). This Court in *Janus* carefully set forth the elements that a plaintiff must establish to prove a fraudulent statement claim under Section 10(b) of the Exchange Act and Rule 10b-5(b). The D.C. Circuit's decision below allows the SEC and private plaintiffs to sidestep *Janus*'s carefully drawn elements of fraudulent statement claims merely by relabeling the claims -- with nothing more -- as fraudulent scheme claims.

The D.C. Circuit's decision imposing primary liability on Petitioner for ministerial conduct that was neither deceptive nor manipulative is contrary to the text of Section 10(b) and this Court's holding in *Central Bank* that a "plaintiff may not bring a 10b-5 suit against a defendant for acts not prohibited by the text of §10(b)") *Central Bank of Denver, N. A. v. First Interstate Bank of Denver, N. A.*, 511 U.S. 164, 173 (1994) The SEC's claims against Petitioner for fraudulent scheme liability based on his nondeceptive conduct extend Rules 10b-5(a) and (c) beyond the scope of Section 10(b). Lorenzo's nondeceptive ministerial conduct also falls outside of Section 17(a)(1)'s

proscriptions against employing "any device, scheme. or artifice to defraud."

The D.C. Circuit's decision also erases the important distinction between primary and secondary violations of the securities laws and opens up large numbers of defendants who are secondary actors at best to claims for primary violations of the securities laws. Permitting primary scheme liability to be imposed on Lorenzo based on statements he did not make would significantly broaden the categories of defendants who can be targeted for primary liability in both SEC actions and private actions. All of these newly at-risk defendants would be secondary players at best. To permit scheme liability "to attach to individuals who did no more than facilitate preparation of material misrepresentations or omissions actually communicated by others ... would swallow the bright-line test between primary and secondary liability." *SEC v. PIMCO Advisors Fund Management LLC*, 341 F. Supp. 2d 454, 467 (S.D.N.Y. 2004); *see also SEC v. Kelly*, 817 F. Supp. 2d 340, 343-44 (S.D.N.Y. 2011).

Here, Petitioner was at most a secondary actor who assisted his boss Gregg Lorenzo (no relation to Petitioner Francis Lorenzo) in sending the two emails in question. Congress has constructed a well thought out statutory scheme whereby the SEC may bring claims for aiding and abetting under Section 20(e) of the Exchange Act (15 U.S. Code § 78t(e)) and the D.C. Circuit's decision upsets this balance. In addition, the D.C. Circuit's decision opens up large numbers of defendants to claims for primary violations of the federal security laws – claims that would otherwise be barred in private litigation under the holding of *Central*

Bank, which eliminated aiding and abetting liability in private securities fraud litigation and in SEC enforcement actions. (*Stoneridge Investment Partners, LLC*, 552 U.S. 148, 167-68, 173 n.7 (2008) (Stevens, J., dissenting); *In the Matter of John P. Flannery and James D. Hopkins*, SEC Release No. 3981, 2014 WL 7145625, at *15, n. 73, *vacated on other grounds*, *Flannery v. SEC*, 810 F.3d 1 (1st Cir. 2012) (acknowledging that *Central Bank* requires the SEC to distinguish between primary and secondary liability).

Facts

In February 2009, Petitioner Francis V. Lorenzo ("Lorenzo") became the director of investment banking at Charles Vista, LLC ("Charles Vista"). (Pet. App. 3). Petitioner has never had a securities violation in his 28 year career. (Lorenzo Hearing Testimony, Joint Appendix ("JA") 312) Charles Vista was a broker-dealer registered with the SEC and owned by Gregg Lorenzo. (Pet. App. 3.) One of Charles Vista's clients was Waste2Energy Holdings, Inc. ("W2E"). W2E represented to Charles Vista and to the public that it had developed a valuable "gasification" technology that could generate electricity by converting solid waste into gas. (*Ibid.*) W2E was a public company with various SEC filings publicly available that described its operations and financial condition in detail. (Pet. App 4).

In September 2009, W2E conducted a private offering of $15 million in convertible debentures to select investors. (Pet. App. 3). Debentures are "debt secured only by the debtor's earning power, not by a lien on any specific asset." BLACK'S LAW DICTIONARY 486 (10th ed. 2014). Charles Vista

served as the exclusive placement agent for W2E's debenture offering. (Pet. App. 3-4).

In its most recent SEC filing at the time, the June 3, 2009 Form 8-K (which is used to notify investors of certain specified material events), W2E stated that its intangible assets, including its gasification technology, were worth just over $10 million as of the end of 2008. (Pet. App. 4). On September 9, 2009, W2E prepared a private offering memorandum for potential investors that described the offering, the debentures and W2E's financial condition. (*Ibid.*)

W2E's gasification technology never materialized and on October 1, 2009, after a lengthy audit, W2E filed an amended Form 8-K, in which it reported a total "impairment" of its intangible assets, because management made a determination that the company's assets were of no value. (Pet. App. 3-4). W2E reduced the value of its gasification technology to zero and its total assets to $370,552 as of March 31, 2009. (Pet. App. 4). On the same day that it filed its amended Form 8-K, October 1, 2009, W2E also filed a quarterly Form 10-Q with the SEC, in which it valued its total assets at $660,408 as of June 30, 2009. (*Ibid.*)

Later on October 1, 2009, Lorenzo's secretary alerted him by email that W2E had filed an amended Form 8-K. (Pet. App. 4). The next day, Lorenzo emailed links to both of W2E's October 1 filings to all Charles Vista brokers. (*Ibid.*) There is no evidence that Lorenzo read the two SEC filings in detail or that he was aware that W2E had written down the value of its assets.

On October 14, 2009, Lorenzo sent two emails within seconds of each other to two potential investors containing "several key points" about W2E's pending debenture offering. (Pet. App. 5, JA 403-06). His emails were copy and pasted from his boss. (JA 244). Lorenzo testified that he sent the emails without thinking about the contents. (Pet. App. 38, 61 and 109). Petitioner did not know or interact with the two recipients of the email. (JA 174-75; 317-19). In fact, one of the two potential investors testified that the Petitioner's email went to his spam account. (JA 172-73). Petitioner never followed up with either individual because the two individuals were not his clients as they were clients of other Registered Representatives of the firm. (JA 322). His emails omitted any mention of the devaluation of W2E's intangible assets. Lorenzo's emails stated to both recipients that the offering came with "3 layers of protection: (I) [W2E] has over $10 mm in confirmed assets; (II) [W2E] has purchase orders and LOI's for over $43 mm in orders; (III) Charles Vista has agreed to raise additional monies to repay these Debenture holders (if necessary)." (Pet. App. 5, JA 403-06) One of Lorenzo's messages said that it had been sent "[a]t the request of Gregg Lorenzo," and the other stated that it had been sent "[a]t the request of Adam Spero [a broker with Charles Vista] and Gregg Lorenzo." In both messages, Lorenzo stated that the recipients could call him with any questions. He signed both messages with his name and title as "Vice President – Investment Banking." (*Ibid.*) Neither recipient of Petitioner's emails invested as a result of Petitioner's email. (JA 175; 317-19)

3. On February 15, 2013, the SEC commenced enforcement proceedings against Petitioner, Gregg

Lorenzo, and Charles Vista by issuing an Order Instituting Proceedings ("OIP"). (Pet. App. 5; OIP at JA 15-39). The OIP, which started the proceedings and is the administrative equivalent of a complaint, did not distinguish between the various subsections of the antifraud provisions of the securities laws and merely charged each respondent with violating Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

Gregg Lorenzo and Charles Vista settled the charges against them. Under the terms of the settlement Gregg Lorenzo was permanently barred from the securities industry and he and Charles Vista were jointly ordered to pay disgorgement of $130,000 and prejudgment interest of $20,000. In addition, Gregg Lorenzo was ordered to pay a civil penalty of $375,000 and Charles Vista was ordered to pay a civil penalty of $4,350,000. See the Commission's Order *In the Matter of Gregg Lorenzo et al.*, SEC Release No. 33-9480, 2013 WL 6087352 (Nov. 20, 2013).

Petitioner did not settle with the SEC and the claims against him concerning the two emails proceeded to an administrative hearing before an SEC administrative law judge. (Pet. App. 5-6). On September 18 and 19, 2013, an administrative hearing was held before the administrative law judge, and, on December 31, 2013, an Initial Decision was rendered (Pet. App. 98-121). After hearing Petitioner's testimony and weighing his credibility, the judge concluded that Petitioner's boss (Gregg Lorenzo) had "drafted" the emails in question (Pet. App. 106) and that Petitioner's boss had "asked" Petitioner to send the emails to the two clients. (Pet. App. 38; 106). The

administrative law judge also concluded that Petitioner did not read the text of the emails and that Petitioner "sent the emails without even thinking about the contents." (Pet. App. 38; 109). Furthermore, the judge noted that the emails themselves expressly stated that they were being sent at "the request" of Petitioner's boss. (Pet. App. 39; 107). "Those factual findings were very favorable to [Francis] Lorenzo and should have cleared Lorenzo of any serious wrongdoing under the securities laws." (Kavanaugh, J., dissenting) (Pet. App. 39).

"Nevertheless, [t]he judge somehow concluded that those findings of fact demonstrated that Lorenzo willfully violated the securities laws – meaning that Lorenzo acted with an intent to deceive, manipulate, or defraud." (Kavanaugh, J dissenting) (Pet. App. 39). The administrative law judge's decision, like the OIP, did not distinguish between any of the subsections of the antifraud provisions and merely concluded that Petitioner violated Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

As a sanction, the judge: (i) ordered Lorenzo to cease and desist from violating each securities-fraud provision giving rise to the charges against him; (ii) imposed against Lorenzo a lifetime bar from the securities industry; and (iii) imposed a civil monetary penalty of $15,000. (Pet. App 39; 119; 120).

> However, the administrative law judge's factual findings and legal conclusions do not square up. If Lorenzo did not draft the emails, did not think about the contents of the emails, and sent the emails only at the behest of his boss, it is impossible to find that Lorenzo acted 'willfully'.

> That is Men's Rea 101. Establishing that a defendant acted willfully in this context requires proof at least of the defendant's 'intent to deceive, manipulate, or defraud.' *Dolphin & Bradbury, Inc. v. SEC*, 512 F.3d 634, 639 (D.C. Cir. 2008) (internal quotation marks omitted)." (Kavanaugh, J., dissenting) (Pet. App. 39).

4. Lorenzo petitioned the Commission for review of the Initial Decision and argued that the administrative law judge's factual findings did not support the judge's legal conclusions and sanctions. The Commission came to the same conclusion. "But instead of vacating the order against Lorenzo, the Commission did something quite different and quite remarkable. In a Houdini-like move, the Commission rewrote the administrative law judge's factual findings to make those factual findings correspond to the legal conclusion that Lorenzo was guilty and deserving of a lifetime suspension." (Kavanaugh, J., dissenting) (Pet. App. 41).

> Without hearing from Lorenzo or any other witnesses, the Commission simply swept the judge's factual and credibility findings under the rug. The Commission concluded that Lorenzo himself was 'responsible' for the emails' contents. . . Faced with inconvenient factual findings that would make it hard to uphold the sanctions against Lorenzo, the Commission – without hearing any testimony – simply manufactured a new assessment of Lorenzo's credibility and rewrote the judge's factual findings. (Kavanaugh, J., dissenting) (Pet. App. 41-42).

On April 29, 2015, the Commission issued an Opinion sustaining the Initial Decision's conclusion. The Commission's opinion did distinguish between the various subsections of the antifraud provisions and held that the two emails in question violated Section 17(a)(1) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5(a), (b) and (c) thereunder (Pet. App. 62-77). The Commission Opinion made no findings with regards to Section 17(a)(2) or (3) The Commission Opinion imposed on Lorenzo a cease-and-desist order, a lifetime bar from the securities industry and a civil monetary penalty of $15,000. (Pet. App. 51-97). The Commission denied Lorenzo's motion for reconsideration on June 3, 2015. (Pet. App. 6). The appeal to the D.C. Circuit followed.

5. On September 15, 2017, the D.C. Circuit overturned the Commission's finding that Lorenzo violated Rule 10b-5(b) on the grounds that under *Janus* Lorenzo did not make the misstatements at issue and vacated the Commission's sanctions. (Pet. App. 1-37). However, the D.C. Circuit in a 2-1 decision upheld the Commission's findings that Lorenzo violated Section 17(a)(1) of the Securities Act, Section 10(b) of the Securities Exchange Act, and Rule 10b-5(a) and (c). (Pet. App. 25). Judge Kavanaugh issued a dissenting opinion that sharply disagreed with the majority's holding that Lorenzo violated any of those securities fraud provisions. In particular, Judge Kavanaugh criticized the majority's deference to the Commission's finding that Lorenzo acted with scienter. "How could Lorenzo have intentionally deceived the clients when he did not draft the emails, did not think about the contents of the emails, and sent the emails only at his boss's direction?" (Kavanaugh, J., dissenting) (Pet.

App. 39-40) Judge Kavanaugh in his dissent also noted that the majority decision is inconsistent when it holds on one hand that Petitioner transmitted statements written by his boss and at his boss's direction and on the other hand also holds that Petitioner engaged in a scheme to defraud solely because of the statements made by Petitioner's boss. (Pet. App. 48)

Judge Kavanaugh was also highly critical of the majority's deference to the Commission's rewriting of the administrative law judge's factual findings. Judge Kavanaugh stated

> Lorenzo was the only relevant witness at trial . . . and given that his credibility was central to the case, the SEC had no reasonable basis to run roughshod over the administrative law judge's findings of fact and credibility assessments. In short, the SEC's rewriting of the findings of fact deserves judicial repudiation, not judicial deference or respect. (Kavanaugh, J., dissenting)(Pet. App. 45)

In fact, Judge Kavanaugh severely criticized the Commission's entire administrative process in the way it handled the enforcement proceedings against Lorenzo. "The administrative law judge's decision in this case contravenes basic due process (Pet. App. 40). . . Lorenzo is entitled to a fair process just like everyone else. He has not received a fair process in this case." (Kavanaugh, J., dissenting)(Pet. App. 40, 49)(citations omitted)

The D.C. Circuit remanded the case to the Commission for reconsideration of the appropriate penalties to impose on Petitioner. "Because we cannot

be certain what role, if any, the Commission's misperception that Lorenzo was the "maker" of the false statements ultimately played in its choice of sanctions, we must remand to enable it to reassess the appropriate penalties." (Internal citations and quotations omitted)(Pet. App. 35-36). The Petition for a Writ of Certiorari was filed on January 26, 2018. This Court granted the petition for a Writ of Certiorari on June 18, 2018. The Commission has not yet issued a decision regarding the sanctions it will impose on Petitioner pursuant to the remand from the D.C. Circuit.

SUMMARY OF ARGUMENT

The D.C. Circuit majority incorrectly held that Petitioner violated Section 17(a)(1) of the Securities Act, Section 10(b) of the Exchange Act and Rules 10b-5(a) and (c)

1. In *Janus* this Court held that only defendants who make a misstatement may be held primarily liable for violations of Section 10(b) and Rule 10b-5(b). The D.C. Circuit's opinion allows the SEC to sidestep the standards that this Court set for misstatement claims in *Janus*. Under the D.C. Circuit's decision the SEC may bring inadequate fraudulent statement claims merely by relabeling them as fraudulent scheme claims. This result renders *Janus's* standards for misstatement claims meaningless. (*See Kelly*, 817 F. Supp. 2d at 344)("Where the primary purpose and effect of a purported scheme is to make a public misrepresentation or omission, courts have routinely rejected the SEC's attempt to bypass the elements necessary to impose 'misstatement' liability under subsection (b) by labeling the alleged misconduct a 'scheme' rather than a 'misstatement.'")

2. The D.C. Circuit's decision also takes an overly broad view of primary liability and virtually eliminates the distinction between primary and secondary liability under the securities laws. To allow the SEC to use a fraudulent scheme theory to pursue primary liability against a defendant who did not make a misstatement would erase the distinction between primary and secondary liability. This, in turn, would allow the SEC to pursue primary liability against defendants that are really secondary actors at best. In the context of private securities litigation the D.C. Circuit's decision would allow private plaintiffs to bring claims against defendants that would otherwise be barred as aiding and abetting claims. *See Global Crossing Ltd. Sec. Litig.*, 322 F. Supp. 2d 319, 337 n.17 (S.D.N.Y. 2004) (Subsections (a) and (c) may only be used to state a claim . . . for the underlying deceptive devices or frauds themselves, and not as a short cut to circumvent *Central Bank*'s limitations on liability for a secondary actor's involvement in making misleading statements. (*quoting In re Lernout & Hauspie Sec. Litig.*, 230 F. Supp. 2d 152, 175 (D. Mass. 2002))). Here, the SEC's interpretation of Rule 10b-5(a) and (c) and each subsection of Section 17(a) blurs the difference between a person with primary liability and an aider and abettor. The SEC's interpretation is also inconsistent with *Janus* because *Janus* intended to "draw a clean line between" those who are primarily liable and those who are secondarily liable. *Janus*, 564 U.S. at 143 n.6 (2011). The theory of "scheme" liability advanced by the SEC is virtually indistinguishable from aiding-and-abetting liability, which is not alleged by the SEC in this matter. The D.C. Circuit decision would allow the SEC and private plaintiffs to relabel conduct that was previously deemed aiding and abetting as

"primary" participation in a fraudulent "scheme." The SEC's scheme theory of liability would also effectively render *Central Bank* a nullity. Under the SEC's reasoning there is no distinction between the Petitioner's ministerial acts and "giving aid to a person who commits a manipulative or deceptive act", the precise conduct held to be outside the scope of Section 10(b) in *Central Bank*, 511 U.S. at 177. Thus, the exact conduct that was previously denominated as aiding and abetting – providing "substantial assistance", with scienter, to a primary violator – could in essentially every case be relabeled through artful pleading as participation in a scheme to defraud. For all practical purposes, *Janus* and *Central Bank* would be invalidated by pulling defendants who are at best aiders and abettors into primary liability. This type of broad primary liability was exactly what the Court rejected in *Janus*. "First Derivative's rule would create the broad liability that we rejected in *Stoneridge*." (*Janus*, 564 U.S. at 146)

3. The D.C. Circuit's decision is not consistent with the text of the antifraud provisions because Lorenzo did not engage in any inherently deceptive or manipulative conduct by sending the emails drafted by his boss. "The language of § 10(b) gives no indication that Congress meant to prohibit any conduct not involving manipulation or deception." *Santa Fe Industries, Inc. v. Green*, 430 U.S. 462, 473 (1977). Here, there is no allegation that Petitioner engaged in manipulative trading practices. In addition, Petitioner did not "use" or "employ" a deceptive or fraudulent scheme because he only copied and pasted language drafted by his boss and such conduct is outside of the active conduct implied by the words "using" or "employing" a deceptive

or fraudulent scheme. The panel majority did not find that Petitioner engaged in any conduct that itself was deceptive or manipulative.

A primary principle that has defined this Court's jurisprudence under Section 10(b) is that in determining "the scope of conduct prohibited by § 10(b), the text of the statute controls." *Central Bank*, 511 U.S. at 173, 177. "It is inconsistent with settled methodology in § 10(b) cases to extend liability beyond the scope of conduct prohibited by the statutory text." *Id.* at 177. This Court's precedents have established three principles regarding the scope of Section 10(b). First, the plain language of the statute prohibits only "manipulative or deceptive" acts, and private plaintiffs may not bring actions under Rule 10b-5 for conduct not prohibited by the statute. Second, the term "manipulative" is a term of art referring to trading practices that artificially inflate the price of a security. Third, "deceptive" conduct, within the meaning of Section 10(b), requires deception - namely, a misstatement or failure to disclose by one who has a duty to disclose. That is why this Court held unequivocally in *Central Bank* that "the statute prohibits only the making of a material misstatement (or omission) or the commission of a manipulative act." *Central Bank*, 511 U.S. at 177.

This Court has made clear that Rule 10b-5 does not go beyond the parameters of Section 10(b). *See Central Bank*, 511 U.S. at 173 (a "plaintiff may not bring a 10b-5 suit against a defendant for acts not prohibited by the text of §10(b)"); *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 200 and 214 (1976)(the "scope [of Rule 10b-5] cannot exceed the power granted the Commission by

Congress under § 10(b)"). Because Petitioner did not engage in manipulative or deceptive conduct -- and did not make the misstatements at issue -- his conduct does not satisfy the requirements for Section 10(b) liability and Rule 10b-5(a) and (c)'s scheme language cannot provide a basis for liability here. Likewise, the lack of any deceptive conduct by Petitioner precludes liability under Section 17(a)(1), which similarly talks of employing devices, schemes and artifices to defraud.

4. Overturning the D.C. Circuit's decision that Petitioner was a primary violator of Section 10(b), Rules 10b-5(a) and (c) and Section 17(a)(1) would not harm the SEC's enforcement program because Congress has provided the SEC with other effective remedies for the conduct at issue. Petitioner's transmission of the two emails that his boss Gregg Lorenzo wrote makes Petitioner a secondary actor at best in this case. Section 20(e) of the Exchange Act is entitled "Prosecution of persons who aid and abet violations" and authorizes the Commission to bring aiding and abetting charges against secondary actors. Section 20(e) authorizes the SEC, but not private plaintiffs, to bring an action against secondary actors who knowingly provide substantial assistance to a primary violator of the securities laws. Section 20(e) was passed by Congress in 1995 as part of the Private Securities Litigation Reform Act, Pub. L. 104-69, 109 Stat. 737 (Dec. 22, 1995) ("PSLRA") and in response to *Central Bank*'s elimination of aiding and abetting liability in private actions under Section 10(b).

In addition to the general authority the Commission has to bring aiding and abetting cases under Section 20(e) other provisions of the Exchange Act expressly

authorize the SEC to bring enforcement cases against associated persons of broker-dealers such as Petitioner. Sections 15(b)(4)(E) and 15(b)(6) of the Exchange Act grants the SEC express statutory authority to file civil enforcement actions against registered broker-dealers and their associated persons who "willfully aided, abetted, counseled, commanded, induced, or procured" violations of the securities laws. 15 U.S.C. §§ 78o(b)(4)(E) and 78o(b)(6)(A). Under these provisions the SEC may suspend for up to twelve months or permanently bar any person associated with a broker or dealer who "has willfully aided, [and] abetted" any violation of the securities laws. 15 U.S.C. §§ 78o(b)(6)(A), 78o(b)(4)(E). Under Section 21B of the Exchange Act, the SEC may also impose monetary penalties against persons who have "willfully aided, [and] abetted" another's violation of the securities laws. 15 U.S.C. § 78u–2(a)(2). However, these aiding and abetting statutes are not at issue in this proceeding because the SEC chose to pursue Petitioner as a primary violator and not as an aider and abettor.

ARGUMENT

I. The D.C. Circuit Majority Decision Renders *Janus's* Standards for Misstatement Liability Meaningless

A. The Statutory and Regulatory Text

"'[T]he starting point in every case involving construction of a statute is the language itself.'" *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 197 (1976)(*quoting Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 756 (1975)). The Court has specifically emphasized

"[a]dherence to the text in defining the conduct covered by § 10(b)." *Central Bank*, 511 U.S. at 174.

The statutory and regulatory framework of the antifraud provision of the federal securities laws prohibit two classes of misconduct in connection with the purchase and sale of securities – fraudulent misstatements and omissions on one hand and fraudulent schemes and conduct on the other. Fraudulent misstatements and omissions are proscribed by Section 10(b), Rule 10(b)-5(b), and Section 17(a)(2). Fraudulent conduct is proscribed by Section 10(b), Rules 10b-5(a) and (c) and Sections 17(a)(1) and (3).

Specifically, Section 10(b) makes it "unlawful for any person directly or indirectly . . . to use or employ, in connection with the purchase or sale of any security . . . any manipulative or deceptive device or contrivance in contravention of" Commission rules. Rule 10b-5 implements the Commission's authority under Section 10(b) through three subsections.

Rule 10b-5(b) makes it unlawful for "any person to make any untrue statement of material fact..." Subsections (a) and (c) of Rule 10b–5 pertain to what courts have termed "scheme liability." Subsections (a) and (c) make it "unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange, (a) To employ any device, scheme, or artifice to defraud, [c. ... (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security." Section 17(a)(1) similarly makes it unlawful

for "any person...to employ any device, scheme or artifice to defraud."

Liability under Rule 10b-5 cannot extend beyond conduct included in Section 10(b)'s prohibitions. Section 10(b)'s prohibition encompasses only acts that are "themselves manipulative or deceptive." Accordingly, only conduct that is itself manipulative or deceptive violates Rule 10b-5. *See Flannery*, 2014 WL 7145625, at *12; *see also In the Matter of Robert W. Armstrong, III*, Exchange Act Release No. 51920, 2005 WL 1498425, at *6 (June 24, 2005); *In the Matter of Leslie A. Arouh*, Exchange Act Release No. 50889, 2004 WL 2964652, at *5 (Dec. 20, 2004).

Courts have described Section 17(a)'s proscriptions as "substantially identical" to those in Rule 10b-5. *See, e.g., Landry v. All Am. Assurance Co.*, 688 F.2d 381, 386 (5th Cir. 1982); *SEC v. Monarch Funding Corp.*, 192 F.3d 295, 308 (2d Cir. 1999) ("Essentially the same elements are required under Section 17(a)(1)-(3) in connection with the offer or sale of a security" as under Rule 10b-5, "though no showing of scienter is required . . . under [Section 17](a)(2) or (a)(3)."); *SEC v. First Jersey Sec., Inc.*, 101 F.3d 1450, 1467 (2d Cir. 1996) ("With respect to § 17(a)(1), essentially the same elements [as in a Rule 10b–5 claim] must be established in connection with the offer or sale of a security."). Other cases also equate the elements of a Rule 10b-5 violation and a Section 17(a) violation. The exceptions are that negligence is sufficient for a violation of Section 17(a)(2) and (3) and that Section 17(a) applies in the offer or sale of a security rather than in connection with a purchase or sale. *See SEC v. Pentagon Capital Mgmt. PLC*, 725 F.3d 279, 285 (2d

Cir. 2013) ("The requirements for a violation of Section 17(a) apply only to a sale of securities but in other respects are the same as Section 10(b) and Rule 10b-5, except" for the different mental state requirements); *SEC v. Morgan Keegan & Co.*, 678 F.3d 1233, 1244 (11th Cir. 2012); *SEC v. Washington Cnty. Util. Dist.*, 676 F.2d 218, 225 (6th Cir. 1982) ("[I]t is axiomatic that, with regard to conduct affecting the sale of securities, Rule 10b-5(2) and Sec. 17(a)(2) are coterminous, except to the degree that proof of scienter is required by Rule 10b-5(2)."). *See also Flannery*, 2014 WL 7145625, at *15 n.79.

B. The *Janus* Court Held Only Defendants who Make Misstatements Can Be Primarily Liable Under Section 10(b) and Rule 10b-5(b)

This Court in *Janus* established a bright-line test to determine the circumstances under which a defendant can be held primarily liable for misstatements under Section 10(b) of the Exchange Act and Rule 10b-5(b) thereunder. *Janus* held that a defendant may be held primarily liable under Rule 10b-5(b) only if the defendant was the "maker" of the misstatement. *Janus*, 564 U.S. 142-43.

In *Janus*, investors in the Janus Investment Fund (the "Fund") brought suit under Section 10(b) of the Exchange Act and Rule 10b-5 against the Fund's adviser and administrator, Janus Capital Management LLC ("JCM") alleging that false statements were made in the Fund's prospectuses. JCM was alleged to have helped prepare the prospectuses at issue and disseminated them to investors through JCG's website. This Court dismissed the case against JCM on the

ground that only the Fund -- and not JCM -- "made" the allegedly improper statements.

> For purposes of Rule 10b–5, the maker of a statement is the person or entity with ultimate authority over the statement, including its content and whether and how to communicate it. Without control, a person or entity can merely suggest what to say, not "make" a statement in its own right. One who prepares or publishes a statement on behalf of another is not its maker. And in the ordinary case, attribution within a statement or implicit from surrounding circumstances is strong evidence that a statement was made by—and only by—the party to whom it is attributed. This rule might best be exemplified by the relationship between a speechwriter and a speaker. Even when a speechwriter drafts a speech, the content is entirely within the control of the person who delivers it. And it is the speaker who takes credit—or blame—for what is ultimately said. *Janus*, 564 U.S. at 142-43 (2011)

In this case the D.C. Circuit correctly held that Petitioner did not make the misstatements at issue and that the maker was Petitioner's boss Gregg Lorenzo. "Voluminous testimony established that [Petitioner] transmitted statements devised by Gregg Lorenzo at Gregg Lorenzo's direction... [and] under the test set forth in *Janus*, Gregg Lorenzo, and not [Petitioner], was "the maker" of the false statements in the emails.")(Pet. App. 17) As a result the D.C. Circuit correctly vacated that part of the Commission decision that found Lorenzo had violated Rule 10b-5(b).

C. The D.C. Circuit Majority Erroneously Held that Lorenzo's Ministerial Acts in Forwarding An Email to Two People Provided a Basis for Fraudulent Scheme Liability

The D.C. Circuit erred when it held that even though Petitioner was not the "maker" of the statements at issue he could nonetheless still be held primarily liable for violating Section 10(b), Rules 10b-5(a) and (c) and Section 17(a)(1) because his ministerial conduct in sending the two emails seconds apart was enough, without anything more, to make Lorenzo a primary violator of these provisions. "Although Lorenzo does not qualify as the "maker" of those statements under *Janus* because he lacked ultimate authority over their content and dissemination, his own active "'role in producing and sending the emails constituted employing a deceptive 'device,' 'act,' or 'artifice to defraud' for purposes of liability under Section 10(b), Rule 10b-5(a) and (c), and Section 17(a)(1)." (Pet. App. 21) However, two emails, which the Petitioner didn't draft or read, sent seconds apart to two people Petitioner did not know cannot be defined as an "active role" in producing and sending the emails, particularly here where Petitioner made no follow up phone calls and neither person invested as a result of the emails.

According to the panel majority Petitioner's "active role" in producing and sending the two emails consisted only of: (i) "produc[ing] email messages containing false statements and [sending] them directly to potential investors expressly in his capacity as head of the Investment Banking Division" (Pet. App. 20); and

(ii) "produc[ing] email messages containing three false statements about a pending offering, [sending] the messages directly to potential investors, and encourag[ing] them to contact him personally with any questions." (*Ibid.*) Allowing such ministerial conduct to serve as the basis for claims is problematic for two reasons. First, the conduct by Petitioner the D.C. Circuit majority cites is not in itself deceptive and therefore cannot support the conclusion that Petitioner employed a deceptive device, act or artifice to defraud. Second, allowing such ministerial conduct to qualify as a deceptive device, act or artifice to defraud would render *Janus* meaningless because misstatement claims that do not meet the standards set forth in *Janus* can merely be relabeled, with nothing more, to qualify as claims for deceptive conduct under Section 17(a)(1), 10(b) and Rules 10b-5(a) and (c).

In fact, the *Janus* Court specifically rejected the notion that these types of ministerial acts that assist another in making a statement could be the grounds for liability under Rule 10b-5(b). Defendants who "contribute "substantial assistance" to the making of a statement but do not actually make it" cannot be held primarily liable under the securities laws. *Janus*, 564 U.S. at 143.

Moreover, there is nothing in the *Janus* decision to suggest that its reasoning should be restricted to just subsection (b) of Rule 10b-5. The misconduct that the SEC alleged against Lorenzo involves no more than his facilitation of the distribution of misstatements that were made by others. To allow Lorenzo's ministerial conduct to serve as the basis for scheme liability would render *Janus*'s distinction between claims for

misstatements and claims for fraudulent acts and schemes meaningless. The D.C. Circuit's holding improperly allows the SEC and private plaintiffs to sidestep the restrictions the *Janus* Court placed on misstatement claims under Rule 10b-5(b) by simply relabeling the claims as fraudulent schemes and pursuing them under Rule 10b-(a) and (c) and Section 17(a)(1). "Where the primary purpose and effect of a purported scheme is to make a public misrepresentation or omission, courts have routinely rejected the SEC's attempt to bypass the elements necessary to impose 'misstatement' liability under subsection (b) by labeling the alleged misconduct a 'scheme' rather than a 'misstatement.'" *Kelly*, 817 F. Supp. 2d at 344.

D. Mere Misstatements By Themselves Cannot Be The Basis of Fraudulent Scheme Claims Under the Federal Securities Laws

The D.C. Circuit's decision conflicts with the text and structure of the federal securities laws and regulations. In framing Section 17, Congress separately prohibited the use of "any device, scheme, or artifice to defraud," *see* § 17(a)(1), obtaining money or property "by means of any untrue statement of a material fact or any omission," *id.* § 17(a)(2), and "engag[ing] in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser," *id.* § 17(a)(3). The Commission divided the conduct prohibited by Rule 10(b)-5 into prohibitions against misstatements (contained in Rule 10b-5(b)) and prohibitions against fraudulent schemes (contained in Rule 10b-5(a) and

(c)). In doing so, both are best understood to have been prohibiting discrete actions—each subsection is understood to be performing different work. Unsurprisingly, before the decision below, courts have always treated misstatements as distinct from claims involving manipulation and fraudulent schemes. *Desai*, 573 F.3d at 940 ("We must recognize, however, that manipulative conduct has always been distinct from actionable omissions").

Under the D.C. Circuit's approach, all claims for false statements could be brought as fraudulent scheme claims, and, vice-versa, claims for nondisclosure of a defendant's fraudulent conduct become viable claims for misstatements and omissions. *Desai*, 573 F.3d at 940. This result conflicts with the well-established rule that statutes and rules should be construed so that effect is given to all their provisions, so that no part will be inoperative or superfluous, void or insignificant. *Hibbs v. Winn*, 542 U.S. 88, 101 (2004) (*quoted in Corley v. United States*, 556 U.S. 303, 314 (2009)).

In addition, there is nothing in the *Janus* decision to suggest that its holding is limited to just Rule 10b-5(b) and not the other subsections. To the contrary, the *Janus* decision did not limit its assessment of the fund adviser's potential liability under Rule 10b-5 to subpart (b) only and there are many places in the opinion where the Court equated liability for making a false statement to liability under Rule 10b-5 generally. For example, in the opinion's very first paragraph, the Court framed the discussion broadly, stating that "[t]his case requires us to determine whether Janus Capital Management LLC (JCM), a mutual fund investment adviser, can be held liable in a private

action under Securities and Exchange Commission (SEC) Rule 10b–5 for false statements included in its client mutual funds' prospectuses." The Court's holding was also broad when it said "[w]e conclude that JCM cannot be held liable because it did not make the statements in the prospectuses."

The Second, Ninth and Eighth Circuits have all held that to have a viable fraudulent scheme claim a plaintiff must prove that the defendant committed an inherently deceptive or manipulative act that is *independent* from any alleged misstatement. This prevents plaintiffs from having a backdoor into liability against defendants who did not make misstatements. *See Lentell v. Merrill Lynch & Co.*, 396 F.3d 161, 177 (2d Cir. 2005) (rejecting scheme liability where the sole basis for such claims is alleged misrepresentations or omissions); *see also PIMCO*, 341 F. Supp. 2d at 468-69 (rejecting scheme liability for market timing, because the fraud arose only from misleading disclosures). "Subsections (a) and (c) are not a backdoor into liability for those who help others make a false statement or omission in violation of subsection (b) of Rule 10b-5." *In re Parmalat Sec. Litig.*, 376 F. Supp. 2d 472, 503 (S.D.N.Y 2005). "Because the core misconduct alleged is in fact a misstatement, it would be improper to impose primary liability . . . by designating the alleged fraud a manipulative device rather than a misstatement." *SEC v. KPMG LLP*, 412 F. Supp. 2d 349, 378 (S.D.N.Y. 2006); *SEC v. Benger*, No. 09 C 676, 2013 WL 1150587, at *5 (N.D. Ill. Mar. 21, 2013)(*Janus* cannot be skirted simply by artful pleading and rechristening a 10b-5(b) claim as a claim under 10b-5(a) and (c)). However, here Petitioner committed no other actions apart from sending the two emails, which

contained statements he did not author, and, therefore, he cannot have engaged in a scheme.

The Second Circuit was the first circuit to address whether misstatements by themselves could form the basis for claims for fraudulent schemes under Section 10(b) of the Exchange Act and Rule 10b-5(a) and (c). In *Lentell v. Merrill Lynch & Co.*, 396 F.3d 161, 177 (2d Cir. 2005), the Second Circuit held that misstatements alone could not form the basis of fraudulent scheme claims. In *Lentell*, the Second Circuit held that the plaintiffs failed to make out fraudulent scheme claims for market manipulation under Rule 10b-5(a) and (c) when the sole basis for the market manipulation claims were alleged misrepresentations or omissions made by the defendants. *See also SEC v. Kelly*, 817 F. Supp. 2d 340, 343-44 (S.D.N.Y. 2011)(dismissing the SEC's fraudulent scheme claims under Rule 10b-5(a) and (c) and 17(a)(2), because they were premised on a misrepresentation and neither defendant "made" the misstatement as *Janus* requires).

The Ninth Circuit in *Desai v. Deutsche Bank Sec., Ltd.*, 573 F.3d 931, 939 (9th Cir. 2009) has also held that mere misstatements standing alone cannot be the basis of claims for fraudulent schemes.

> We must recognize, however, that manipulative conduct has always been distinct from actionable omissions. Omissions are generally actionable under Rule 10b-5(b)... Manipulative conduct, by contrast, is actionable under Rule 10b-5(a) or (c) and includes activities designed to affect the price of a security artificially by simulating market activity that does not reflect genuine investor demand....If such nondisclosure of a

> defendant's fraud was an actionable omission, then every manipulative conduct case would become an omissions case. If that were so, then all of the Supreme Court's discussion of what constitutes manipulative activity would be redundant. We decline to read the Supreme Court's case law on manipulative conduct as a little more than an entertaining, but completely superfluous, intellectual exercise. *See Stoneridge*, 128 S.Ct. at 769 (listing the three types of §10(b) actions); *Cent. Bank*, 511 U.S. at 177, 114 S.Ct. 1439 (same)(citations omitted). (*Desai*, 573 F.3d at 939).

In a difference case, the Ninth Circuit held that, for fraudulent scheme claims to be actionable under Rule 10b-5(a) or (c), something more is required than just deceptive statements. *WPP Luxembourg Gamma Three Sarl v. Spot Runner, Inc.*, 655 F.3d 1039 (9th Cir. 2011). In *WPP* the Ninth Circuit held that a "defendant may only be liable as part of a fraudulent scheme based upon misrepresentations and omissions under Rules 10b–5(a) or (c) when *the scheme also encompasses conduct beyond those misrepresentations or omissions.*" (655 F.3d at 1057)(emphasis added). In the *WPP* case, the Ninth Circuit also stated that a "theory of recovery that merely repeats the allegations made in support of ... misrepresentation and omission claim" is not a valid claim under Rule 10b–5(a) or (c). 655 F.3d at 1057-58 (*citing In re Nat'l Century Fin. Enters., Inc. Inv. Litig.*, 2006 WL 469468, at *21 (S.D.Ohio Feb. 27, 2006)). Moreover, "[c]ourts have generally held that a Rule 10b–5(a) and/or (c) claim cannot be premised on the alleged misrepresentations or omissions that form the basis of a Rule 10b–5(b)

claim." (*WPP*, 655 F.3d at 1057). Therefore, here, even if Petitioner was the maker of the statements in the two emails, which he was not, the SEC could still not establish a scheme claim because the SEC's scheme claim is based on nothing more than Petitioner's transmission of the misstatements in the two emails.

The Eighth Circuit is in agreement with the Ninth and Second Circuits in holding that misstatements, standing alone, can never be sufficient to bring a fraudulent scheme claim under Rule 10b-5(a) or (c). In *Public Pension Fund Group v. KV Pharmaceutical Co.*, 679 F.3d 972 (8th Cir. 2012), the Eighth Circuit stated that "[w]e join the Second and Ninth Circuits in recognizing a scheme liability claim must be based on conduct beyond misrepresentations or omissions actionable under Rule 10b-5(b)." (679 F.3d at 987). In doing so, the Eighth Circuit recognized the important distinction between claims for misstatements and claims for deceptive schemes. "Claims brought under Rules 10b-5(a) and (c) are generally referred to as 'scheme liability' claims." 679 F.3d at 986 (citing *DVI, Inc.*, 639 F.3d 623, 643 n. 29).

In contrast to this majority rule, the Eleventh Circuit in *SEC v. Big Apple Consulting USA, Inc.*, 783 F.3d 786 (11th Cir. 2015) held that "even a person ... who is not the 'maker' of an untrue statement of material fact, nonetheless could be liable as a primary violator of Rule 10b–5(a) and (c)." (783 F.3d 795-96) and that "[S]ubsection (b) was the only subsection at issue in *Janus*" (783 F.3d at 796). *See also SEC v. Monterosso*, 756 F.3d 1326, 1334 (11th Cir. 2014)("*Janus* only discussed what it means to 'make' a statement for purposes of Rule 10b–5(b) and did not

concern section 17(a)(1) or (3) or Rule 10b–5(a) or (c)" and that "the operative language of section 17(a) does not require a defendant to "make" a statement in order to be liable." (756 F.3d at 1334). Big Apple Consulting was an investor relations firm that provided investor and public relation services to microcap companies. *Big Apple*, 783 F.3d at 790. One of its clients was a small public company called CyberKey Solutions, Inc. CyberKey paid for Big Apple's services with shares of its stock. Over the course of several months Big Apple provided the public with false information related to a purported multimillion dollar purchase order that CyberKey had received from the Department of Homeland Security. The information about the false order artificially inflated the price of the stock and Big Apple sold hundreds of millions of CyberKey shares for proceeds of almost $8 million. *Big Apple*, 783 F.3d at 793-94.

Petitioner submits that the 11th Circuit's position is erroneous and inconsistent with this Court's precedent. In addition, the *Big Apple* case involved facts that are significantly different than the facts here including Big Apple's receipt of almost $8 million over the course of several months from widely disseminated false information. In contrast, Petitioner sent an email to two investors seconds apart and received only $150 when one of the investors later decided to invest through his broker.

II. The D.C. Circuit's Decision Erases the Distinction between Primary and Secondary Liability and Greatly Expands the Number of Defendants Who Qualify as Primary Violators

A. The D.C. Circuit's Holding is Inconsistent With this Court's Precedent in *Central Bank*, *Stoneridge* and *Janus*

The D.C. Circuit majority's holding that Petitioner can be held responsible as a primary violator of the securities laws under a fraudulent scheme theory constitutes an overly expansive view of primary liability under the securities laws and is inconsistent with this Court's holdings in *Central Bank*, *Stoneridge* and *Janus*. This Court has repeatedly rejected the broad reading of primary liability that the SEC is now pursuing.

> For decades . . .the SEC has tried to erase that distinction [between primary and secondary liability] so as to expand the scope of primary liability under the securities laws. For decades, the Supreme Court has pushed back hard against the SEC's attempts to unilaterally rewrite the law. *See Janus*, 564 U.S. 135; *Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc.* 552 U.S. 148 (2008); *Central Bank of Denver, NIA. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164 (1994). Still undeterred in the wake of that body of Supreme Court precedent, the SEC has continued to push the envelope and has tried to circumvent those Supreme Court decisions. *See, e.g., In the Matter*

of John P. Flannery & James D. Hopkins, Release No. 3981 (Dec. 15, 2014). This case is merely the latest example. (Kavanaugh, J., dissenting) (Pet. App. 47).

1. *Central Bank* Held that There is No Cause of Action for Aiding and Abetting under Section 10(b)

Central Bank held there was no cause of action for aiding and abetting in private lawsuits and established a clear rule limiting liability under Section 10(b) to those persons who themselves make a misstatement (or omission in the face of a duty to disclose) or engage in manipulative trading. *Central Bank*, 511 U.S. at 177 ("As in earlier cases considering conduct prohibited by Section 10(b), we again conclude that the statute prohibits only the making of a material misstatement (or omission) or the commission of a manipulative act."). Turning to the language of Section 10(b), the Court "reach[ed] the uncontroversial conclusion . . . that the text of the 1934 Act does not itself reach those who aid and abet a § 10(b) violation". *Id.* at 177.

In *Central Bank* a public building authority in Colorado issued $26 million in bonds and Central Bank of Denver served as the indenture trustee on the bonds. The plaintiffs alleged that the disclosure document for the bonds contained a misrepresentation about the appraisal of the land that secured the bonds. The plaintiffs further alleged that Central Bank had obtained an appraisal showing that the property values were declining and that the appraisal of the land securing the bonds was no longer accurate. The plaintiff's alleged that even though Central Bank was obligated to ensure that the building authority was in

a sound financial position the bank had delayed an independent review of the appraisal. The Court had to address the question of whether Central Bank was liable to the purchasers of the bonds on a legal theory of aiding and abetting. The Court held that Section 10(b) liability did not extend to aiders and abettors because the scope of Section 10(b) was strictly limited by the statute's text, which does not refer to aiding and abetting liability. *Central Bank*, 511 U.S. at 173. *Central Bank* thus reaffirmed that liability under section 10(b) is limited to those who *themselves* actually make a material misstatement or violate a duty to disclose, or who employ a manipulative device as that term of art has been interpreted and not those who simply aid and abet. The holding in *Central Bank* applies to SEC enforcement actions as well as to private lawsuits. *Stoneridge*, 552 U.S. at 167-68, 173 n.7 (Stevens, J., dissenting); *Flannery*, 2014 WL 7145625, at *15, n.73 (acknowledging that *Central Bank* requires the SEC to distinguish between primary and secondary liability).

The theory of "scheme" liability advanced by the SEC for primary liability is almost indistinguishable from aiding and abetting liability, which *Central Bank* rejected. The circuit courts that have addressed arguments virtually identical to the SEC's arguments have ruled that a secondary actor like Petitioner who neither makes a misstatement (or omission in the face of a duty to disclose) nor employs a manipulative device may not be held liable as primary violators under Section 10(b), even if the defendant is alleged to have participated in some manner in a scheme to defraud. *See Regents of Univ. of Cal. v. Credit Suisse First Boston (USA), Inc.*, 482 F.3d 372, 388 (5th Cir. 2007)

("'[D]eceptive' conduct involves either a misstatement or a failure to disclose by one who has a duty to disclose." (internal quotation marks omitted)). In *Central Bank*, this Court held that Section 10(b) prohibits only the making of a material misstatement (or omission) or the commission of a manipulative act. *In re Charter Communications, Inc., Sec. Litig.*, 443 F.3d 987, 992 (8th Cir. 2006), *aff'd by Stoneridge*, 552 U.S. 148 (2008) ("[A]ny defendant who does not make or affirmatively cause to be made a fraudulent misstatement or omission, or who does not directly engage in manipulative securities trading practices, is at most guilty of aiding and abetting and cannot be held liable under § 10(b) or any subpart of Rule 10b-5."); *Anixter v. Home-Stake Prod. Co.*, 77 F.3d 1215, 1226 (10th Cir. 1996)("[W]e conclude that in order for accountants to 'use or employ' a 'deception' actionable under the antifraud law, they must themselves make a false or misleading statement (or omission) that they know or should know will reach potential investors.").

In response to *Central Bank*'s elimination of aiding and abetting liability in 1995 Congress passed Section 20(e) of the Exchange Act as part of the PSLRA. Section 20(e) restored the SEC's ability to bring actions for aiding and abetting against anyone who "knowingly or recklessly provides substantial assistance to another person" in a violation of the federal securities laws. Section 20(e) did not restore the ability of private plaintiffs to bring aiding and abetting claims. The D.C. Circuit's ruling that Petitioner was a primary violator of the antifraud provisions represents and overly expansive view of primary liability and is inconsistent with Section 20(e)'s well-considered definition of an aider and abettor as one who substantially assists

another in committing a primary violation. The D.C. Circuit's decision converts Petitioner, who is a secondary actor at best, into a primary violator and extends primary liability well beyond the boundaries set by this Congress.

2. *Stoneridge* Rejected a Broad Theory of Primary Liability Like the One the SEC is Pursuing

This Court again rejected a broad test for primary liability in *Stoneridge*. In *Stoneridge* the plaintiffs alleged that Charter Communications, a large publicly traded cable television company, falsely inflated its revenues by entering into sham contracts with various vendors that allowed Charter Communications to record inflated revenue and postpone recognizing certain corporate expenses. The plaintiffs alleged that the vendors could be held primarily liable under Section 10(b) and Rule 10b-5(a) and (c) because the vendors themselves participated in a "scheme or artifice to defraud" and by engaging in a "course of business which operates . . . as a fraud or deceit." The Eighth Circuit held that *Central Bank* barred the plaintiffs' claims against the vendors. "Any defendant who does not make or affirmatively cause to be made a fraudulent misstatement or omission, or who does not directly engage in manipulative securities trading practices, is at most guilty of aiding and abetting and cannot be held liable under § 10(b) or any subpart of Rule 10b-5."

This Court affirmed and drew a sharp distinction between the person who made the misstatements (Charter Communications) and the vendors who played some role in facilitating the false statements. This

Court in *Stoneridge* held that the vendors were secondary actors whose involvement was too remote to satisfy the requirement of reliance. The *Stoneridge* Court held that holding the suppliers liable as primary actors would exceed the boundaries of primary liability that the Court set around Section 10(b). Part of the *Stoneridge* Court's reasoning was that the plaintiffs' arguments in favor of primary liability would contravene *Central Bank* and Section 20(e) by converting aiders and abettors into primary violators.

> Petitioner's theory, moreover, would put an unsupportable interpretation on Congress' specific response to *Central Bank* in § 104 of the PSLRA. Congress amended the securities laws to provide for limited coverage of aiders and abettors. Aiding and abetting liability is authorized in actions brought by the SEC but not by private parties. *See* 15 U.S.C. § 78t(e). Petitioner's view of primary liability makes any aider and abettor liable under § 10(b) if he or she committed a deceptive act in the process of providing assistance. . . . Were we to adopt this construction of § 10(b), it would revive in substance the implied cause of action against all aiders and abettors except those who committed no deceptive act in the process of facilitating the fraud; and we would undermine Congress' determination that this class of defendants should be pursued by the SEC and not by private litigants. *Stoneridge*, 552 U.S. at 162-63.

Like in *Stoneridge*, this Court too should draw a sharp distinction between the person who made the misstatements (here, Petitioner's boss) and the person

who had a secondary role in disseminating the statements by email (Petitioner) and hold that Petitioner cannot be held liable as a primary violator of the securities laws.

3. *Janus* Drew a Clean Line Between Those Who Are Primarily Liable and Those Who are Secondary Actors

In *Janus*, this Court again refused to extend the scope of actors who can qualify as primary defendants in claims for misstatements by holding that only those who "made" a misstatement can be liable for the misstatement. *Janus* expressed significant concern with a broad interpretation of who could qualify as the maker of a statement because of the need to maintain the distinction between primary and secondary liability. "A broader reading of 'make,' including persons or entities without ultimate control over the content of a statement, would substantially undermine *Central Bank*. If persons or entities without control over the content of a statement could be considered primary violators who 'made' the statement, then aiders and abettors would be almost nonexistent." *Janus*, 564 U.S. at 143. The *Janus* Court also indicated that it intended to "draw a clean line between" those who are primarily liable and those who are secondarily liable. *Janus*, 564 U.S. at 143 n.6.

The *Janus* Court invoked *Stoneridge* to reject broader tests for primary liability from both the government as amici and the plaintiffs themselves. The brief from the Department of Justice urged this standard:

> [A] person makes a false or misleading statement and thus can be liable as a primary violator of Rule 10b-5 when that person creates the statement, which occurs when the statement is written or spoken by him, or if he provides the false or misleading information that another person then puts into the statement, or if he allows the statement to be attributed to him. (Brief for the United States as Amici Curiae Supporting Respondent, Janus, 2010 WL 4339892, at *13 (emphasis, quotation marks, and citation omitted)).

Janus squarely rejected that argument. The *Janus* Court cited *Stoneridge* in rejecting the expansive standards offered by the government:

> Adopting the Government's definition of "make" would also lead to results inconsistent with our precedent. The Government's definition would permit private plaintiffs to sue a person who "provides the false or misleading information that another person then puts into the statement." . . . But in *Stoneridge*, we rejected a private Rule 10b-5 suit against companies involved in deceptive transactions, even when information about those transactions was later incorporated into false public statements. . . . We see no reason to treat participating in the drafting of a false statement differently from engaging in deceptive transactions, when each is merely an undisclosed act preceding the decision of an independent entity to make a public statement. *Janus*, 564 U.S. 144-45.

Thus, *Janus* rejected this broad theory of liability, holding that the rules proposed by the government "would create the broad liability that we rejected in *Stoneridge*." (*Janus*, 564 U.S. at 146); Andrew N. Vollmer, *SEC Revanchism and the Expansion of Primary Liability Under Section 17(a) and Rule 10b-5*, 10 Va. L. & Bus. Rev. 273 (2016).

Stoneridge and *Janus* thus establish this Court's view that primary liability under Rule 10b-5 is confined within boundaries and does not extend to all persons with some connection to false information received by an investor. The *Janus* Court's discussion of *Stoneridge* also demonstrates that the Court's reasoning in *Janus* was not limited to an interpretation of just subsection (b) of Rule 10b-5. In fact, the analysis and reasoning in *Stoneridge* applied to all of Rule 10b-5.

The Court has already expressed frustration about the SEC's persistently broad position on primarily liability. "This also is not the first time this Court has disagreed with the SEC's broad view of §10(b) or Rule 10b–5. *See, e.g., Central Bank of Denver, N. A. v. First Interstate Bank of Denver, N. A.*, 511 U.S. 164, 188–191 (1994); *Dirks v. SEC*, 463 U.S. 646, 666, n. 27 (1983); *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 207 (1976); *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 746, n. 10 (1975)." (*Janus*, 564 at 145, n. 8). In *Central Bank* the Court rejected the SEC's policy arguments in support of a broad 10b-5 aiding and abetting cause of action (*Central Bank*, 511 U.S. 164, 188–191) and in *Hochfelder* the Court rejected the SEC's arguments that negligence could be the basis of liability under Rule 10b-5. (*Hochfelder*, 425 U.S. 185, 207).

The holding of the D.C. Circuit majority converts every aider and abettor into a primary violator and this is not consistent with decades of this Court's precedent. If allowed to stand, the D.C. Circuit's decision would make *Central Bank, Stoneridge* and *Janus* irrelevant because every peripheral actor would be a primary violator.

The panel majority's expansive view of primarily liability also undermines Congress's well considered statutory scheme of primary and secondary liability. The D.C. Circuit majority decision allows the SEC "to evade the important statutory distinction between primary liability and secondary (aiding and abetting) liability. After all, if those who aid and abet a misstatement are themselves primary violators for engaging in a scheme to defraud, what would be the point of the distinction between primary and secondary liability?" (Kavanaugh, J., dissenting) (Pet. App. 46) Section 20(e) allows the SEC to bring actions for aiding and abetting against anyone who "knowingly or recklessly provides substantial assistance to another person" in a violation of the federal securities laws. The D.C. Circuit's expansive view of primary liability would permit the SEC to bring primary liability claims against defendants who did no more than provide substantial assistance to another person who violated the securities laws, which is the very definition of aiding and abetting.

B. The Distinction Between Primary and Secondary Liability is Important in SEC Enforcement Cases Because SEC Claims for Aiding and Abetting Have Different Elements Than Claims for Primary Violations

The distinction between primary and secondary liability is important in SEC enforcement actions such as this one because the express statutory provisions permitting the SEC to bring aiding and abetting claims have different elements than claims for primary liability under Section 10(b), Rule 10b-5(a) and (c) and Section 17(a)(1). In order for a defendant to be liable as an aider and abettor in an SEC civil enforcement action, the SEC must prove: "(1) the existence of a securities law violation by the primary (as opposed to the aiding and abetting) party; (2) 'knowledge' of this violation on the part of the aider and abettor; and (3) 'substantial assistance' by the aider and abettor in the achievement of the primary violation." *SEC v. Apuzzo*, 689 F.3d 204, 206 (2nd Cir. 2012). The distinction between primary and secondary liability also matters a great deal for private securities lawsuits because private plaintiffs may not maintain aiding and abetting lawsuits. *Central Bank*, 511 U.S. at 191.

However, instead of maintaining the important limitations on secondary liability, the D.C. Circuit majority created a backdoor by which plaintiffs – both the SEC and private plaintiffs – can bring claims of primary violations of the securities laws under a scheme liability theory against large numbers of defendants who would otherwise be secondary actors in

SEC actions and immune from suit by private plaintiffs.

In Section 20(e) Congress authorized the SEC to pursue aiders and abettors – but only as aiders and abettors who provide "substantial assistance" – not as primary violators. The D.C. Circuit decision allowing the SEC to pursue Petitioner as a primary violator completely erases the distinction between primary and secondary liability that this Court has put in place *in Central Bank, Stoneridge* and *Janus*. The D.C. Circuit's decision also contravenes the lines Congress has established for primary and secondary liability in Section 20(e). In Section 20(e) Congress drew the line between an aider and abettor and a primary violator. Congress has spoken in Section 20(e) and an aider and abettor is a person who substantially assists a primary violation. Therefore, the conduct of a primary violator must be more than just merely providing substantial assistance, which at best is all Petitioner did when he sent the emails at issue at the direction of his boss.

C. The SEC Could Have Brought This Action Against Petitioner as an Aider and Abettor But Chose Not to Do So

The SEC has aggressively tried to expand the scope of primary liability under the securities laws even though it is empowered by Section 20(e) of the Exchange Act to bring civil actions against aiders and abettors of securities fraud. Allowing the SEC to repackage inadequate claims for misstatements as fraudulent scheme claims allows the SEC to be able to evade the important statutory distinction between primary liability and secondary (aiding and abetting) liability under Section 20(e) of the Exchange Act by

charging aiders and abettors with primary liability under a theory of scheme liability.

In this case the SEC could have brought an action under Section 20(e) of the Exchange Act against Lorenzo for aiding and abetting violations of the antifraud provisions by Gregg Lorenzo, who was Francis Lorenzo's boss and the maker of the misstatements in the two emails that were sent. While Lorenzo would have factual defenses to an SEC action for aiding and abetting, such a claim would not have raised any of the problematic legal questions that are the subject of this petition.

Nevertheless, the SEC chose not to bring aiding and abetting claims against Lorenzo and instead improperly pursued primary liability claims under a theory of scheme liability. By doing so the SEC chose to evade the important limitations that this Court has placed on securities fraud liability in *Janus*, *Stoneridge* and *Central Bank*. This Court should not permit the SEC to evade the carefully laid out elements of misstatement claims and statutory aiding and abetting claims.

Permitting primary scheme liability to be imposed on Lorenzo based on statements he did not make would also significantly broaden the categories of defendants who can be targeted for primary liability in both SEC actions and private actions. All of these newly at-risk defendants would be secondary players at best. "To attach to individuals who did no more than facilitate preparation of material misrepresentations or omissions actually communicated by others ... would swallow the bright-line test between primary and

secondary liability." *PIMCO*, 341 F. Supp. 2d at 467; *see also Kelly*, 817 F. Supp. 2d at 343.

III. THE DECISION BELOW CONFLICTS WITH THE TEXT OF SECTION 10(b) AND 17(a) BECAUSE LORENZO DID NOT EMPLOY A MANIPULATIVE DEVICE OR CONTRIVANCE, NOR DID HE EMPLOY A DEVICE, SCHEME, OR ARTIFICE TO DEFRAUD

In addition to undermining this Court's precedents, the decision below cannot be reconciled with the text of Section 10(b) and Section 17(a). Petitioner did not violate Section 10(b) because his conduct does not meet the definition of "deception" or "manipulation" under Section 10(b). Petitioner also did not violate Rule 10b-5 for the same reason, because Rule 10b-5 cannot impose liability beyond the scope of Section 10(b) itself. In addition, Petitioner did not violate *either* Section 10(b) *or* Section 17(a)(1) because he did not "use" or "employ" a manipulative, deceptive or fraudulent device or scheme. This statutory language refers to active misconduct going beyond mere support to another or aiding and abetting a violation.

A. This Court Has Defined the Terms "Deception" and "Manipulation" in Section 10(b), and Petitioner's Conduct Does Not Meet the Definitions

Section 10(b) make it unlawful "[t]o use or employ, in connection with the purchase or sale of any security . . . *any manipulative or deceptive device or contrivance* in contravention of such rules and regulations as the Commission may prescribe." (emphasis added). The

"statute prohibits only the making of a material misstatement (or omission) or the commission of a manipulative act. . . . We cannot amend the statute to create liability for acts that are not themselves manipulative or deceptive within the meaning of the statute." *Central Bank*, 511 U.S. at 177- 78 (1994). *Central Bank* also stated that the "it is inconsistent with settled methodology in § 10(b) cases to extend liability beyond the scope of conduct prohibited by the statutory text." *Id.* at 175, 177. The *Central Bank* Court further stated it has "refused to allow 10b-5 challenges to conduct not prohibited by the text of the statute." *Id.* at 173.

The SEC's rule making authority under Section 10(b) is constrained by the text of the statute and Rule 10b-5 cannot extend liability beyond the statutory text.

> The rulemaking power granted to an administrative agency charged with the administration of a federal statute is not the power to make law . . . Thus, despite the broad view of the Rule advanced by the [SEC] in this case, *its scope can not exceed the power granted the [SEC] by Congress under § 10(b)." Hochfelder*, 425 U.S. at 213-14 (emphasis added).

In *Santa Fe Industries v. Green*, 430 U.S. 462 (1977) the Court squarely held that Rule 10b-5 liability cannot go beyond the text of Section 10(b) when it rejected a claim that a breach of fiduciary duty without deception or manipulation fell under Section 10(b)'s prohibitions. In that case plaintiffs were minority shareholders who brought an action to recover a higher price per share after the defendant majority shareholder forced the plaintiffs to sell their shares in a merger transaction.

The Second Circuit had allowed the plaintiffs' claim to proceed and held that a Rule 10b-5 action could be premised on "breaches of fiduciary duty by a majority against minority shareholders without any charge of misrepresentation or lack of disclosure". *Santa Fe,* 430 U.S. at 470. The Second Circuit specifically referenced Rule 10b-5(a) and (c) and stated

> [An] erroneous assumption is that in order to allege a claim under Rule 10b-5 there must be some showing of misrepresentation or lack of disclosure. . . . But only subdivision [b] of 10b-5 deals with nondisclosure and misrepresentation. The Rule contains two other subdivisions which state explicitly that fraud other than and in addition to a failure to disclose or truthfully represent is also actionable. . . . It must be that the failure to observe this broader scope of Rule 10b-5 led the court below to dismiss the complaint . . . lest there be any lingering doubt on this point, we now hold that in such cases, including the one now before us, no allegation or proof of misrepresentation or nondisclosure is necessary. *Green v. Santa Fe Industries, Inc.,* 533 F.2d 1283, 1286-87 (2nd Cir. 1976).

This Court reversed. The Court concluded that "[t]he language of § 10(b) gives no indication that Congress meant to prohibit any conduct not involving manipulation or deception". *Santa Fe,* 430 U.S. at 473. The *Santa Fe* Court also held that the term manipulation "is 'virtually a term of art when used in connection with securities markets'" that "'refers generally to practices, such as wash sales, matched orders, or rigged prices, that are intended to mislead

investors by artificially affecting market activity". *Id.* at 476 (quoting *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 199 (1976)). Here, there has been no allegation that Petitioner engaged in manipulative conduct. In *Chiarella v. United States*, 445 U.S. 222 (1980) the Court addressed the concept of deception and the Court refused to extend the concept of "deception" beyond the basic common law categories of misrepresentation or a duty to disclose, holding that "[w]hen an allegation of fraud is based upon nondisclosure, there can be no fraud absent a duty to speak . . . premised upon a duty to disclose arising from a relationship of trust and confidence between the parties to a transaction." 445 U.S. 235, 230. The *Chiarella* Court expressly held that the need for either a misrepresentation or a duty to disclose is an essential element of liability under Rules 10b-5(a) or (c). *See* Daniel A McLaughlin, *Liability Under Rules 10b-5(a) and (c)*, 31 Del. J. Corp. Law 631, 636 (2006).

The holdings in *Santa Fe* and *Chiarella* made clear that under Rules 10b-5(a) and (c), just as under Rule 10b-5(b), liability cannot extend beyond three categories: (1) the making of a misrepresentation, (2) an omission or nondisclosure coupled with a duty to speak, and (3) the commission of a manipulative act. Here the SEC relies on the absence of any reference to the word "make" in subsections (a) and (c) of Rule 10b-5 and Section 17(a)(1). However, the essential elements of a Section 10(b) claim, namely a misrepresentation, duty to disclose or execution of a manipulative trade, are still required by Section 10(b) itself when pursuing a claim under Rule 10b-5(a) or (c).

Several district courts have also held that claims under Rules 10b-5(a) and (c) require either a material misstatement or the commission of a manipulative act. For example, in *In re Dynegy, Inc. Securities Litigation*, 339 F. Supp. 2d 804, 914-16 (S.D. Tex. 2004) the court dismissed claims against an outside bank that had engaged in transactions that the issuer misrepresented in its financial statements, concluding that

> *Central Bank* precludes liability based on allegations that a group of defendants acted together to violate the securities laws unless each defendant committed a manipulative or deceptive act in furtherance of the scheme. . . . Plaintiffs cannot invoke subsections (a) and (c) of Rule 10b-5 to circumvent *Central Bank*'s limitations on liability for a secondary actor's involvement in the preparation of false and misleading statements.

See also In re Lake States Commodities, 936 F.Supp. 1461, 1471-72 (N.D. Ill. 1996) (rejecting Rule 10b-5(a) & (c) liability in absence of misrepresentation, duty to disclose or claim of manipulation), *abrogated on other grounds*, *Damato v. Hermanson*, 153 F.3d 464 (7th Cir. 1998); *In re Rent-Way Secs. Litig.*, 209 F. Supp. 2d 493, 500, 505 (W.D. Pa. 2002) (rejecting Rule 10b-5(a) & (c) liability against auditor that "improperly reviewed and approved of" quarterly financial statements, where "misstatements are what the Plaintiffs allegedly relied upon to their detriment, and the allegations simply do not permit an inference that Plaintiffs relied upon any 'device,' 'scheme,' 'artifice,' 'act,' 'practice' or 'course of business' employed or engaged in by [the auditor] such that a Rule 10b-5 claim could be established."); *Charal*

Inv. Co. v. Rockefeller, 131 F. Supp. 2d 593, 603 (D. Del. 2001) ("Plaintiffs['] claim pursuant to Rule 10b-5(a) requires a demonstration of materiality even though it is not expressly required in the language of the rule"), *aff'd on other grounds*, 311 F.3d 198 (3d Cir. 2002). *See* collected cases at 31 Del. J. Corp. Law 631, 639 n.32.

In *Lentell v. Merrill Lynch & Co.*, 396 F.3d 161 (2d Cir.), *cert. denied*, 126 S. Ct. 421 (2005) the Court held that claims sounding in misrepresentation or omission are not actionable as "manipulation."

> [P]laintiffs cast their claims in terms of market manipulation, pursuant to Rule 10b-5(a) and (c). We hold that where the sole basis for such claims is alleged misrepresentations or omissions, plaintiffs have not made out a market manipulation claim under Rule 10b-5(a) and (c). *Lentell*, 396 F.3d at 177.

A similar conclusion was reached by the Seventh Circuit in *Foss v. Bear, Stearns & Co.*, 394 F.3d 540 (7th Cir. 2005). In that case the district court rejected plaintiff's claim for Rule 10b-5(a) and (c) liability against a brokerage firm whose employee opened accounts with securities he allegedly knew to be stolen from the plaintiff. On appeal, the Seventh Circuit affirmed, refusing to apply the label of "manipulation" and instead holding that the absence of a misrepresentation made, or duty to disclose owed, by the brokerage firm to the estate was fatal to the claim. "Foss wants us to call the conduct 'manipulation' rather than 'fraud,' but this is a distinction without a difference. In securities law, manipulation is a kind of fraud; deceit remains essential." *Foss v. Bear, Stearns & Co.*, 394 F.3d 540, 542 (7th Cir. 2005) (*citing*

Schreiber v. Burlington N., Inc., 472 U.S. 1 (1985) and *Santa Fe Indus., Inc. v. Green*, 430 U.S. 462, 476-77 (1977)). Just as courts have rejected attempts to repackage misrepresentation claims as manipulation claims, the Court should reject the SEC's argument that claims against Petitioner sounding in misrepresentation can be repackaged as fraudulent schemes.

B. The Decision Below Is Inconsistent with the Text of Sections 10(b) and 17(a)(1) Because Petitioner Did Not Engage in Active Misconduct

The D.C. Circuit majority's theory of liability also cannot be squared with the text of Section 10(b) making it unlawful "*[t]o use or employ*" a "manipulative or deceptive device or contrivance" in violation of SEC rules (emphasis added), or the text of Section 17(a)(1) regarding "*employ[ing]* . . . device[s], scheme[s], or artifice[s] to defraud." The plain language of these provisions requires active misconduct. The defendant must "use or employ" a deceptive device or "make" a false or misleading statement. See *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 200–01, 212–13 (1976) (emphasizing that the statute's language "clearly connotes intentional misconduct"). Merely playing a supporting role does not give rise to liability.

Here, none of Petitioner's conduct can be fairly described as deceptive, fraudulent or playing more than a supportive role. Petitioner did not "use" or "employ" a deceptive or fraudulent scheme, because merely copying and pasting an email from his boss is too passive a role to qualify as "using" or "employing" a deceptive or fraudulent scheme. The panel majority

did not find that Petitioner engaged in any conduct that itself was deceptive or manipulative. Petitioner's purported "active role" in producing and sending the two emails consisted only of "produc[ing] email messages containing false statements and [sending] them directly to potential investors expressly in his capacity as head of the Investment Banking Division" (Pet. App. 20) and "produc[ing] email messages containing three false statements about a pending offering, [sending] the messages directly to potential investors, and encourag[ing] them to contact him personally with any questions." (*Id.* at 21). None of Petitioner's conduct involves him doing anything inherently deceptive or using or employing a manipulative or deceptive device or contrivance. Nor does Petitioner's conduct qualify as the making of a material misstatement, a conclusion that the D.C. Circuit properly rejected under the holding of *Janus*.

IV. OVERTURNING THE D.C. CIRCUIT'S MAJORITY DECISION WOULD NOT HARM THE SEC'S ENFORCEMENT PROGRAM

Overturning the D.C. Circuit's majority decision that Petitioner was a primary violator of Section 10(b), Rules 10b-5(a) and (c) and Section 17(a)(1) would not harm the SEC's enforcement program because Congress has provided the SEC with other remedies for the conduct at issue. Petitioner's transmission of the two emails that his boss Gregg Lorenzo wrote makes Petitioner a secondary actor at best in this case.

As discussed above, Section 20(e) of the Exchange Act authorizes the Commission to bring aiding and abetting charges against secondary actors. In addition to the general authority the Commission has under

20(e) to bring aiding and abetting cases under Section 20(e) other provisions Exchange Act expressly authorize the SEC to bring enforcement cases against associated persons of broker-dealers such as Petitioner. The Exchange Act grants the SEC express statutory authority to file civil enforcement actions against registered broker-dealers and their associated persons who "willfully aided, abetted, counseled, commanded, induced, or procured" violations of the securities laws. 15 U.S.C. §§ 78o(b)(4)(E), 78u-2(a)(2); *see also Central Bank*, 511 U.S. at 183. Under these provisions the SEC may suspend for up to twelve months or permanently bar any person associated with a broker or dealer who "has willfully aided, [and] abetted" any violation of the securities laws. 15 U.S.C. §§ 78o(b)(6)(A), 78o(b)(4)(E). Under Section 21B of the Exchange Act, the SEC may also impose monetary penalties against persons who have "willfully aided, [and] abetted" another's violation of the securities laws. 15 U.S.C. § 78u–2(a)(2). Here, the SEC has not argued that it has had any problems or concerns in pursuing aiding and abetting claims under Section 20(e).

In addition to the SEC's own enforcement powers, it also oversees non-governmental self-regulatory organizations, such as the Financial Industry Regulatory Authority ("FINRA"), which can bring disciplinary actions against securities firms and their employees who aid and abet violations of Section 10(b). FINRA currently regulates all securities firms registered with the SEC. FINRA is empowered to bring aiding and abetting enforcement actions against their member firms and associated persons under FINRA Rule 2010 - Standards of Commercial Honor and Principles of Trade. Overturning the D.C. Circuit's

decision would likewise not hinder the SEC's oversight of FINRA or FINRA's ability to pursue aiding and abetting claims in its own forum.

V. BROAD SCHEME LIABILITY FOR SECONDARY ACTORS WOULD HARM U.S. SECURITIES MARKETS AND IS UNNECESSARY TO DETER MISCONDUCT OR COMPENSATE INVESTORS

The SEC argues that scheme liability is necessary to deter fraud and protect the integrity of the capital markets. Even if that argument is correct it is not determinative. "Policy considerations cannot override" the "text and structure of the Act." *Central Bank*, 511 U.S. at 188. However, the SEC's argument is wrong because scheme liability would harm securities markets, damage the economy, and injure investors, while doing nothing to deter fraud. Insofar as "practical factors" are relevant *(Blue Chip Stamps*, 421 U.S. at 749), "the inexorable broadening" of liability would "result in more harm than good." *Id.* at 747-748. These practical considerations show, as in *Central Bank*, that any decision to expand liability to new classes of defendants should be left to Congress.

As far back as *Ernst & Ernst v. Hochfelder*, the Court rejected a broad remedial view of primary liability under the securities laws because the standard of liability created by a particular section of the Securities Act or Exchange Act must "rest primarily on the language of that section." *Hochfelder*, 425 U.S. at 200. "[G]eneralized references to the remedial purposes" of the securities laws "will not justify reading a provision more broadly than its language and the statutory scheme reasonably permit." *Aaron v. SEC*,

446 U.S. 680, 695 (1980) (*quoting and citing Touche Ross & Co. v. Redington*, 442 U.S. 560, 578 (1979); *SEC v. Sloan*, 436 U.S. 103, 116 (1978)) (internal quotation marks omitted).

Central Bank held that liability under § 10(b) is "'an area that demands certainty and predictability.'" 511 U.S. at 188 (*quoting Pinter v. Dahl*, 486 U.S. 622, 652 (1988)). This is because uncertainty drives up the costs of numerous legitimate transactions and eliminates some altogether. *See* 511 U.S. at 188-89. As the Fifth Circuit stated "[i]n *Central Bank*, the Court emphasized that securities fraud liability is an area of the law that demands certainty and predictability. Secondary liability brings neither; instead it gives rise to confusion about the extent of secondary actors' obligations and invites vague and conflicting standards of proof in divers courts." *Regents of Univ. of Cal. v. Credit Suisse First Boston (USA), Inc.*, 482 F.3d 372, 386 (5th Cir. 2007) (citation omitted). "Strict construction of § 10(b) *against* inputting aiding and abetting liability for secondary actors under the rubric of "deceptive acts" or "schemes" gives rise to the type of certainty that the Court sought in *Central Bank*." *Regents*, 482 F.3d at 392 (emphasis added). Allowing the D.C. Circuit's majority decision to stand in this matter would permit the exact type of uncertainty and unpredictability in the securities markets that *Central Bank* cautioned against.

CONCLUSION

For the foregoing reasons the judgment of the D.C. Circuit should be reversed.

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No. 17-1077

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BRIEF FOR THE RESPONDENT

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QUESTION PRESENTED

Whether, in an enforcement proceeding brought by the Securities and Exchange Commission, a person who knowingly disseminates false or misleading statements in connection with a securities transaction can be found to have violated Section 17(a)(1) of the Securities Act of 1933, 15 U.S.C. 77q(a)(1) (2006); Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. 78j(b) (2006); and Rule 10b-5(a) and (c), 17 C.F.R. 240.10b-5(a) and (c), even if the person does not "make" false or misleading statements within the meaning of Rule 10b-5(b), 17 C.F.R. 240.10b-5(b).

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1-50) is reported at 872 F.3d 578. The opinion and order of the Securities and Exchange Commission (Pet. App. 51-95, 96-97) are reported at 111 SEC Docket 1761 and are available at 2015 WL 1927763. The initial decision of the administrative law judge (Pet. App. 98-121) is reported at 107 SEC Docket 5934 and is available at 2013 WL 6858820.

JURISDICTION

The judgment of the court of appeals was entered on September 29, 2017. On December 19, 2017, the Chief Justice extended the time within which to file a petition for a writ of certiorari to and including January 26, 2018, and the petition was filed on that date. The petition was granted on June 18, 2018. The jurisdiction of this Court rests on 28 U.S.C. 1254(1).

STATUTORY AND REGULATORY PROVISIONS INVOLVED

Pertinent statutory and regulatory provisions are reproduced in the appendix to this brief. App., *infra*, 1a-3a.

STATEMENT

1. In the wake of—and in response to—the 1929 stock market crash, Congress passed the Securities Act of 1933, ch. 38, Tit. I, 48 Stat. 74 (15 U.S.C. 77a *et seq.*), which was "the first experiment in federal regulation of the securities industry," *SEC* v. *Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 198 (1963). With the Securities Act, Congress sought to "provide full and fair disclosure of the character of securities sold in interstate and foreign commerce and through the mails, and to prevent frauds in the sale thereof. "48 Stat. 74. The Securities Act "embodies a flexible rather than a static principle, one that is capable of adaptation to meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits." *SEC* v. *W. J. Howey Co.*, 328 U.S. 293, 299 (1946).

The following year, Congress passed the Securities Exchange Act of 1934, ch. 404, 48 Stat. 881 (15 U.S.C. 78a *et seq.*). The Exchange Act "provide[d] for the regulation of securities exchanges and of over-the-counter markets operating in interstate and foreign commerce and through the mails" and sought "to prevent inequitable and unfair practices on such exchanges and markets." *Ibid.* Those reforms helped to ensure "the maintenance of fair and honest markets in [securities] transactions," § 2, 48 Stat. 882, and to "achieve a high standard of business ethics in the securities industry,"

SEC v. *Zandford*, 535 U.S. 813, 819 (2002) (citation omitted).

Both the Securities Act and the Exchange Act contain antifraud provisions that are at issue in this case. Section 17(a) of the Securities Act makes it

> unlawful for any person in the offer or sale of any securities * * * by the use of any means or instruments of transportation or communication in interstate commerce or by use of the mails, directly or indirectly—
>
> (1) to employ any device, scheme, or artifice to defraud, or
>
> (2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or
>
> (3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

15 U.S.C. 77q(a) (2006).[1]

Section 10(b) of the Exchange Act makes it "unlawful for any person * * * [t]o use or employ, in connection with the purchase or sale of any security * * * , any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the [Securities and Exchange] Commission may prescribe." 15 U.S.C. 78j(b). That provision "was designed as a

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[1] Unless otherwise indicated, all citations to the United States Code refer to the 2006 version, which was the law in force at the time of petitioner's conduct. Subsequent amendments are immaterial to the issues in this case.

catch-all clause to prevent fraudulent practices." *Chiarella* v. *United States*, 445 U.S. 222, 226 (1980). In 1942, the Securities and Exchange Commission (SEC or Commission) adopted Rule 10b-5 to implement Section 10(b). See 7 Fed. Reg. 3804 (May 22, 1942).

Rule 10b-5 provides that:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce * * *
>
> (a) To employ any device, scheme, or artifice to defraud,
>
> (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,
>
> in connection with the purchase or sale of any security.

17 C.F.R. 240.10b-5.

2. Petitioner worked as the director of investment banking at Charles Vista, LLC, a registered broker-dealer that petitioner described as "'a small boiler room'" where representatives "engaged in high-pressure sales tactics" and "seemed to be 'stretching the truth.'" Pet. App. 53-54. During the relevant period, petitioner's only client was Waste2Energy Holdings, Inc. (W2E), a startup seeking to develop a "gasification" technology that could generate electricity from solid waste. *Id.* at 3. W2E's technology "never materialized,"

and the company "sought to escape financial ruin" by offering up to $15 million in convertible debentures—debt secured by the company's potential future earning power rather than by its existing assets. *Ibid.* Charles Vista served as the placement agent for W2E's debenture offering. *Id.* at 3-4.

Petitioner knew that W2E's technology "didn't really work," and that the company's financial condition "was horrible." Pet. App. 55. In June 2009, petitioner referred to W2E's intellectual property as a "dead asset." J.A. 197. On October 1, 2009, W2E submitted SEC filings stating that the company's gasification technology and related assets that it had previously valued at more than $10 million had "no value," and that its total assets amounted to $660,408. Pet. App. 4 (citation omitted). Petitioner "acknowledged that he read the amended" filing on October 1, although "'probably not as closely as [he] should have.'" *Id.* at 10 (citation omitted; brackets omitted). In an email that petitioner received on October 5, W2E's chief financial officer explained that W2E had written off "all of [its] intangible assets" due to its "assessment of the value of what those asset[s] are worth today." *Id.* at 4-5 (citation omitted; brackets in original). Petitioner acknowledged that, by October 2009, he viewed offering W2E's debentures as a "toxic convertible debt spiral." *Id.* at 9 (citation omitted).

Despite knowing about W2E's dire financial condition and prospects, petitioner continued to seek investors for W2E's debenture offering, from which petitioner stood to gain 7%-9% of any funds he raised. Pet. App. 9, 56. On October 14, 2009—two weeks after W2E's filing writing off almost all of its assets—petitioner sent two emails to prospective investors, with the subject line "W2E Debenture Deal Points." *Id.* at

59. The emails stated that "the Investment Banking division of Charles Vista ha[d] summarized several key points of" the W2E debenture offering, including "3 layers of protection: (I) [W2E] has over $10 mm in confirmed assets[;] (II) [W2E] has purchase orders and" letters of intent "for over $43 mm in orders[;] (III) Charles Vista has agreed to raise additional monies to repay these Debenture holders (if necessary)." *Id.* at 107 (emphasis omitted). One email stated that petitioner had sent it "[a]t the request of Gregg Lorenzo," the owner of Charles Vista (who is not related to petitioner). *Id.* at 5 (brackets in original); see *id.* at 3. The other email stated that it had been sent "[a]t the request of" a Charles Vista broker and Gregg Lorenzo. *Ibid.* (brackets in original). Petitioner signed both messages with his name and title as "Vice President—Investment Banking," and the emails stated that potential investors should contact him if they had any questions. *Ibid.*; see *id.* at 107-108 (reproducing full text of email).

Petitioner later offered inconsistent accounts of the creation of the emails. At one point, he stated that he did not "recall" discussing "either of the e-mails or the subject matter of the e-mails at all with Gregg Lorenzo." J.A. 249. At another point, he claimed that "Gregg Lorenzo asked [him] to send" the emails to potential investors. J.A. 350. Petitioner also said that he thought he had "authored" the emails that were then "approved by" Gregg Lorenzo and a compliance officer, while at the same time asserting that all three men had "authored" the emails. J.A. 247; see J.A. 302.

Petitioner testified that, before he sent his emails, he was aware "that the $10 million asset had been written off." J.A. 240. Petitioner also conceded that, by Sep-

tember 2009—before he sent the emails—he did not believe that W2E had $43 million in purchase orders and letters of intent, instead testifying that "I didn't think anything was going to come through." J.A. 262. Petitioner further acknowledged that it was misleading to state that Charles Vista had agreed to financially back the debenture holders. J.A. 268-269, 275.

3. a. On February 15, 2013, the Commission instituted administrative and cease-and-desist proceedings against petitioner, Gregg Lorenzo, and Charles Vista. Pet. App. 5. The Commission charged each with violating multiple antifraud provisions: Section 17(a)(1) of the Securities Act, 15 U.S.C. 77q(a)(1); Section 10(b) of the Securities Exchange Act, 15 U.S.C. 78j(b); and Securities Exchange Act Rule 10b-5, 17 C.F.R. 240.10b-5. Pet. App. 5. Gregg Lorenzo and Charles Vista settled the charges against them. *Id.* at 5-6.

Petitioner contested the charges before an SEC administrative law judge (ALJ). After a hearing, the ALJ found that petitioner "knew the truth about W2E's parlous financial condition" when he sent the two emails, which contained representations "staggering" in their "falsity." Pet. App. 108, 113. In describing the scienter element of the relevant antifraud provisions, the ALJ stated that "[r]ecklessness can satisfy the scienter requirement." *Id.* at 111. The ALJ credited petitioner's testimony that petitioner had "sent the emails without even thinking" about the contents. *Id.* at 109. The ALJ concluded, however, that petitioner "was reckless—although he knew that W2E was in terrible financial shape, he sent the emails without thinking." *Id.* at 113. The ALJ explained that, if petitioner had "taken a minute to read the text," he "would have realized that it was false and misleading and that W2E was not worth

anything near what was being represented to potential investors." *Ibid.* The ALJ found that petitioner had "willfully" violated each of the charged provisions "by his material misrepresentations and omissions concerning W2E in the emails." *Id.* at 114.

b. Petitioner sought review before the Commission. The SEC determined that petitioner had violated Rule 10b-5(b) by knowingly making materially false and misleading statements in the two emails that he had sent to prospective investors. Pet. App. 76; see *id.* at 73-76. The Commission also concluded that petitioner had independently violated Section 17(a)(1), Section 10(b), and Rule 10b-5(a) and (c) by knowingly sending "materially misleading language from his own email account to prospective investors." *Id.* at 77. The Commission explained that petitioner's "role in producing and sending the emails constituted employing a deceptive 'device,' 'act,' or 'artifice to defraud' for purposes of liability under" those provisions, "[i]ndependently of whether" petitioner's "involvement in the emails amounted to 'making' the misstatements for purposes of Rule 10b-5(b)." *Ibid.*

In the course of its analysis, the SEC addressed "the question" of scienter—namely, whether [petitioner] knew or must have known that his emails were materially misleading." Pet. App. 68. The Commission concluded that this "standard is met here." *Ibid.* The Commission rejected, as "implausible," petitioner's assertion that he had sent the emails without giving them significant thought, instead finding that petitioner "was well aware that the emails falsely represented crucial facts about W2E and its debenture offering." *Id.* at 73. The Commission further stated that, "if [petitioner] did send the emails without 'think[ing] about it one way or

the other,' as he claims, such a dismissive attitude toward investors' interests would * * * still constitute acting with extreme recklessness." *Ibid.* (second set of brackets in original).

As sanctions, the Commission imposed a cease-and-desist order, a $15,000 civil penalty, and a lifetime bar from the securities industry. Pet. App. 79.

4. Petitioner filed a petition for review in the court of appeals, challenging the Commission's liability determination and its imposition of an industry-wide bar and a $15,000 civil penalty. Pet. App. 7. The court granted the petition in part, vacated the challenged sanctions, and remanded for further proceedings. *Id.* at 36-37.

The court of appeals first held that substantial evidence supported the Commission's determination that the statements in the emails were false or misleading and that petitioner had acted with the requisite scienter. Pet. App. 7-14, 27-31. With respect to scienter, the court observed that, "[u]nlike in his arguments before the ALJ and Commission, [petitioner], in [the court of appeals], d[id] not take the position that he simply passed along statements supplied by Gregg Lorenzo without thinking about them." *Id.* at 28; see *id.* at 22. Rather, the court explained, petitioner had argued in the court that he had lacked scienter because he had believed the emails to be true—an argument that presumed that petitioner was familiar with the emails' content at the time he sent them. *Id.* at 28-30.

The court of appeals next held that petitioner had not violated Rule 10b-5(b) because he did not "make" the misleading statements in the emails. Pet. App. 15. Rather, the court concluded, the "maker" of those statements was petitioner's boss, Gregg Lorenzo. *Id.* at 16. The court of appeals relied on this Court's holding in

Janus Capital Group, Inc. v. *First Derivative Traders*, 564 U.S. 135, 142 (2011), that a person "make[s]" a statement under Rule 10b-5(b) only if he has "ultimate authority over the statement, including its content and whether and how to communicate it." Pet. App. 15. The court concluded that Gregg Lorenzo had "ultimate authority" over the statements in the emails, and that he was therefore "the maker" of the statements for purposes of Rule 10b-5(b). *Id.* at 19 (citation omitted).

The court of appeals further held, however, that petitioner had violated Section 17(a)(1), Section 10(b), and Rule 10b-5(a) and (c). Pet. App. 20-22. The court explained that those provisions, unlike Rule 10b-5(b), do not require that a violator "make" a false statement. *Id.* at 20 (citation omitted). Rather, those provisions prohibit the use of a fraudulent "device," "practice," or "scheme." *Id.* at 20-21 (citations omitted).

The court of appeals held that petitioner's conduct—which included "produc[ing] email messages containing three false statements about a pending offering, sen[ding] the messages directly to potential investors, and encourag[ing] them to contact him personally with any questions"—"fits comfortably within the ordinary understanding of" those prohibitions. Pet. App. 21. The court noted that petitioner had "present[ed] no argument that his actions fail to satisfy the statutory and regulatory language" of Section 17(a)(1), Section 10(b), and Rule 10b-5(a) and (c). *Id.* at 22. The court concluded that, although "[petitioner] was not the 'maker' of the false statements because he lacked ultimate authority over them," he had "'engaged' in a fraudulent 'act' and 'employed' a fraudulent 'device' when, with knowledge of the statements' falsity and an intent to de-

ceive, he sent the statements to potential investors carrying his stamp of approval as investment banking director." *Id.* at 34.

The court of appeals declined "to reach the merits" of petitioner's challenge to the sanctions. Pet. App. 35. Because the court had "no assurance that the Commission would have imposed the same level of penalties in the absence of its finding of liability for making false statements under Rule 10b-5(b)," it vacated the sanctions that the Commission had previously imposed, and it remanded to the agency for further proceedings. *Ibid.*

Judge Kavanaugh dissented. Pet. App. 37-40. He would have vacated the Commission's finding that petitioner had violated Section 17(a)(1), Section 10(b), and Rule 10b-5(a) and (c). *Id.* at 49-50. In his view, liability under those provisions "must be based on conduct that goes beyond a defendant's role in preparing mere misstatements or omissions made by others." *Id.* at 46.

SUMMARY OF ARGUMENT

By knowingly sending emails to investors containing false financial information designed to induce the purchase of securities in his client's company, petitioner engaged in a paradigmatic "device, scheme, or artifice to defraud" and an "act, practice, or course of business which operates as a fraud." 15 U.S.C. 77q(a)(1); 17 C.F.R. 240.10b-5(a) and (c). Under a straightforward interpretation of the statutory and regulatory text, petitioner is liable under Section 17(a)(1) and Rule 10b-5(a) and (c). This Court's longstanding construction of federal fraud laws further underscores that petitioner's conduct falls squarely within the charged provisions.

Petitioner makes no sustained effort to dispute that knowingly sending email messages containing false statements about an issuer's financial health and prospects directly to potential investors is the type of deceptive conduct encompassed by the plain text of Section 17(a)(1) and Rule 10b-5(a) and (c). Instead, he attempts to relitigate the facts regarding his knowledge of the emails' contents. Petitioner's argument in the court of appeals assumed that he had sent the emails with knowledge of their contents. In any event, petitioner offers no basis for disturbing the Commission's factual finding that petitioner sent the emails with the requisite scienter. And petitioner's effort to confine Section 17(a)(1) and Rule 10b-5(a) and (c) to only the particular forms of fraud involved in certain prior decisions has no foundation in the text of the relevant provisions or the prior decisions themselves.

Petitioner's principal contention is that he cannot be liable for disseminating deceptive information to investors under Section 17(a)(1) and Rule 10b-5(a) and (c) because he is not liable for "mak[ing]" misstatements under Rule 10b-5(b). Petitioner's argument relies heavily on this Court's decision in *Janus Capital Group, Inc.* v. *First Derivative Traders*, 564 U.S. 135 (2011), which held that the "maker of a statement" under Rule 10b-5(b) "is the person or entity with ultimate authority over the statement." *Id.* at 142. But in interpreting the term "make" in Rule 10b-5(b), *Janus* did not purport to alter the scope of Section 17(a)(1), Rule 10b-5(a), or Rule 10b-5(c), which do not include that term. Nor is there any logical inconsistency in concluding that the sender of a material misstatement is liable for securities fraud under Section 17(a)(1) and Rule 10b-5(a) and (c)

even if he is not the maker of that misstatement for purposes of Rule 10b-5(b). To the contrary, the common law, the Commission, lower courts, and this Court have long upheld the imposition of liability for fraudulent conduct that involves misstatements even in the absence of liability for making those misstatements.

Petitioner's contention that imposing liability under Section 17(a)(1) and Rule 10b-5(a) and (c) will eliminate the distinction between primary liability and secondary liability articulated by this Court in *Central Bank of Denver, N. A.* v. *First Interstate Bank of Denver, N. A.*, 511 U.S. 164 (1994), and *Stoneridge Investment Partners, LLC* v. *Scientific-Atlanta, Inc.*, 552 U.S. 148 (2008), is misguided for similar reasons. *Central Bank* and *Stoneridge* held that private civil liability under Section 10(b) does not extend to those who aid and abet a primary violator without engaging in any manipulative or deceptive conduct of their own. That principle is not implicated here, because petitioner himself committed deceptive conduct by personally disseminating misstatements directly to potential investors. Treating petitioner as a primary violator enforces the plain meaning of the relevant provisions while preserving the distinction between primary and secondary liability.

No other principle of interpretation supports a departure from the statutory and regulatory text. Petitioner briefly invokes the canon against redundancy, but this Court has repeatedly explained that Congress and the Commission wrote the securities laws to be mutually reinforcing, not mutually exclusive. It is accordingly well accepted that the respective provisions of Section 17(a) and Rule 10b-5 contain some permissible overlap. In any event, the court of appeals concluded that petitioner did *not* violate Rule 10b-5(b) in this case.

Concluding that his conduct instead violated Section 17(a)(1) and Rule 10b-5(a) and (c) would not create any redundancy with Rule 10b-5(b).

Petitioner predicts an onslaught of meritless private suits against defendants who would otherwise be secondary actors insulated from private suits. But Congress has created ample safeguards against meritless private suits in the Private Securities Litigation Reform Act of 1995 (PSLRA), Pub. L. No. 104-67, 109 Stat. 737. Among other requirements, private plaintiffs must satisfy heightened pleading requirements and show reliance on the defendants' misconduct, as well as demonstrating economic loss and loss causation. Interpreting Section 17(a) and Rule 10b-5(a) and (c) according to their plain meaning in this Commission enforcement action would not change any of those requirements.

By contrast, adopting petitioner's theory would significantly undermine enforcement of the securities laws by categorically precluding primary liability in any case involving a misstatement that the defendant himself did not "make." And if the "maker" of the false statement was not primarily liable—because he had acted without scienter, for example—a person who disseminated the statement with fraudulent intent would not be subject to aiding-and-abetting liability either. There is no basis in the text, structure, history, or purpose of the securities laws to create such a loophole. The Court should enforce the plain meaning of Section 17(a) and Rule 10b-5(a) and (c), and uphold the Commission's finding that petitioner is liable for fraud.

ARGUMENT

PETITIONER'S CONDUCT FALLS SQUARELY WITHIN THE CHARGED PROHIBITIONS ON SECURITIES FRAUD

A. Petitioner's Conduct Falls Within The Plain Meaning Of Section 17(a)(1) And Rule 10b-5(a) and (c)

1. "[S]tatutory text controls the definition of conduct covered by" the antifraud provisions of the federal securities laws. *Central Bank of Denver, N. A.* v. *First Interstate Bank of Denver, N. A.*, 511 U.S. 164, 175 (1994); see *Morrison* v. *National Austl. Bank Ltd.*, 561 U.S. 247, 261 n.5 (2010). Thus, "the starting point in every case involving" the scope of securities fraud "is the language" of the statute. *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 197 (1976) (brackets and citation omitted). When "the terms of a statute [are] unambiguous, judicial inquiry is complete." *Rubin* v. *United States*, 449 U.S. 424, 430 (1981). The "language of [the] statute controls." *Hochfelder*, 425 U.S. at 201.

Here, the controlling language comes from two statutes and one rule. Section 17(a)(1) of the Securities Act makes it unlawful "to employ any device, scheme, or artifice to defraud" in offering or selling a security. 15 U.S.C. 77q(a)(1). Section 10(b) of the Exchange Act makes it unlawful to "use or employ, in connection with the purchase or sale of any security * * * any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe." 15 U.S.C. 78j(b).

Rule 10b-5, which implements Section 10(b), imposes three prohibitions "in connection with the purchase or sale of any security." 17 C.F.R. 240.10b-5. Rule 10b-5(a) prohibits "employ[ing] any device, scheme, or artifice to defraud." 17 C.F.R. 240.10b-5(a). Rule 10b-5(b) prohibits "mak[ing] any untrue statement of a

material fact" or "omit[ting] to state a material fact." 17 C.F.R. 240.10b-5(b). And Rule 10b-5(c) prohibits "engag[ing] in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person." 17 C.F.R. 240.10b-5(c).

As the court of appeals correctly held (Pet. App. 20-21), petitioner's knowing dissemination of false information about his client's financial prospects directly to potential investors "fits comfortably within the ordinary understanding of" a "device, scheme, or artifice to defraud" prohibited by the identical language of Section 17(a)(1) and Rule 10b-5(a). 15 U.S.C. 77q(a)(1); 17 C.F.R. 240.10b-5(a). Indeed, petitioner's effort to induce investors to part with their money based on false financial premises is a paradigmatic example of "the type of fraudulent behavior which was meant to be forbidden by the statute and the rule." *SEC* v. *National Sec., Inc.*, 393 U.S. 453, 467 (1969); see, *e.g.*, *Superintendent of Ins. of N.Y.* v. *Bankers Life & Cas. Co.*, 404 U.S. 6, 8-9 (1971) (finding Rule 10b-5 violation where party to a securities transaction was "duped" by false information about corporate assets, which in fact "had been depleted").

Petitioner's dissemination of false information to induce investment also fits comfortably within the dictionary definition of "device, scheme, or artifice to defraud" in Section 17(a)(1) and Rule 10b-5(a). 15 U.S.C. 77q(a)(1); 17 C.F.R. 240.10b-5(a). For purposes of those provisions, a "device" is simply "[t]hat which is devised, or formed by design." *Aaron* v. *SEC*, 446 U.S. 680, 696 n.13 (1980) (quoting *Webster's New International Dictionary* 713 (reprint 1942) (2d ed. 1934) (*Webster's*) (brackets in original). A "scheme" is a "project" or "plan or pro-

gram of something to be done." *Ibid.* (quoting *Webster's* 2234). And an "artifice" is "an artful stratagem or trick." *Ibid.* (quoting *Webster's* 157). Although those definitions may present difficult questions at the margins, petitioner's attempt to deceive investors into backing W2E by sending an email dramatically overstating the company's assets, pending orders, and ability to repay falls within the heartland of "device, scheme, or artifice to defraud."

The relevant history of those terms further demonstrates that petitioner's conduct is covered by Section 17(a)(1) and Rule 10b-5(a). The Senate Report accompanying the Exchange Act identified "the dissemination of false information" as an example of a "device[ ]" that is "subjected to regulation by the Commission," and it equated the "devices" prohibited by Section 10(b) with "manipulative or deceptive practices." S. Rep. No. 792, 73d Cong., 2d Sess. 8-9, 18 (1934). Moreover, even before Congress enacted the securities laws, this Court construed federal fraud statutes prohibiting any "scheme or artifice to defraud" to cover the inducement of financial payment through false "representations as to the past or present, or suggestions and promises as to the future." *Durland* v. *United States*, 161 U.S. 306, 313 (1896); see *Bettman* v. *United States*, 224 F. 819, 824-825 (6th Cir.), cert. denied, 239 U.S. 642 (1915); *Wilson* v. *United States*, 190 F. 427, 432 (2d Cir. 1911); see also *United States* v. *Maze*, 414 U.S. 395, 406 (1974) (noting that, before the enactment of the securities laws, "most criminal prosecutions for fraudulent securities transactions were brought under the" mail fraud statute) (citation omitted).

For the same reasons, petitioner's attempt to induce investment falls squarely within the ordinary meaning

of Rule 10b-5(c), which prohibits "engag[ing] in any act, practice, or course of business which operates or would operate as a fraud." 17 C.F.R. 240.10b-5(c). Attempting to induce investment by sending a message falsely representing a company's financial condition plainly constitutes an "act" or "practice" that "operate[s] as a fraud" on the recipient. *Ibid.*; see, *e.g.*, *Bankers Life*, 404 U.S. at 9 (describing plan to secure investment based on false asset reports as "an 'act' or 'practice' within the meaning of Rule 10b-5").

2. In the court of appeals, petitioner "present[ed] no argument that his actions fail[ed] to satisfy the statutory and regulatory language." Pet. App. 22. Indeed, he did not "examine—or even reference—the text of those provisions in arguing that they should be deemed not to apply to his conduct." *Ibid.* Likewise, petitioner makes no meaningful effort in this Court to explain how the conduct in which he was found to have engaged—knowingly sending emails containing false statements about an issuer's financial health and prospects directly to potential investors—could be thought to fall outside the terms of Section 17(a)(1) and Rule 10b-5(a) and (c). Petitioner's amici similarly disregard the text of those provisions, going so far as to urge that "the different words of the subparts will not assist in resolving this case." Law Professors Amicus Br. 21; but see, *e.g.*, *United States* v. *Naftalin*, 441 U.S. 768, 773-774 (1979) (distinguishing subparts of Section 17(a)); *Affiliated Ute Citizens* v. *United States*, 406 U.S. 128, 152-153 (1972) (distinguishing subparts of Rule 10b-5).

In arguing that his conduct fell outside the coverage of Section 17(a)(1) and Rule 10b-5(a) and (c), petitioner instead challenges the factual premises on which the Commission and the court of appeals decided this case.

He contends (Pet. Br. 26-27) that he "didn't draft or read" the emails, and that his "ministerial" conduct in sending them "is not in itself deceptive." But those assertions squarely contradict petitioner's position in the court of appeals. There, he argued that "at the time the email was sent," he "*believed the statements to be true*," and therefore "did not act with scienter." Pet. App. 28 (brackets and citation omitted); see *id.* at 28-29 (explaining petitioner's argument that he had a "*good faith belief in the veracity of the statements*") (citation omitted). Petitioner could not have believed the statements to be true, as he argued to the court of appeals, if he did not read them, as he argues to this Court. See *id.* at 29 ("[A] person cannot have 'believed statements to be true' at the time he sent them, or possessed a 'good faith belief in their veracity,' if he had given no thought to their content.").

Given petitioner's position below that the substance of the email was accurate, the court of appeals decided the case "on the understanding that" petitioner, "having taken stock of the emails' content and having formed the requisite intent to deceive, conveyed materially false information to prospective investors about a pending securities offering backed by the weight of his office as director of investment banking." Pet. App. 22. This Court should decide the case on the same understanding. See *Wharf (Holdings) Ltd.* v. *United Int'l Holdings, Inc.*, 532 U.S. 588, 593-594 (2001).

Even if petitioner had preserved his current scienter argument below, this Court is not "a court for correction of errors in fact finding." *Exxon Co., U. S. A.* v. *Sofec, Inc.*, 517 U.S. 830, 841 (1996) (citation omitted). And to the extent the Court reviews factual issues, the Com-

mission's findings "if supported by substantial evidence, are conclusive." 15 U.S.C. 78y(a)(4). Petitioner offers no basis for setting aside, under that substantial-evidence standard, the Commission's determination that he was aware of the emails' content at the time he sent them. See Pet. App. 53. And if that determination is treated as controlling, petitioner's intentional dissemination of financial information he knew was false in an attempt to induce investment plainly constitutes a "device, scheme, or artifice to defraud" and an "act, practice, or course of business which operates * * * as a fraud" under Section 17(a)(1) and Rule 10b-5(a) and (c). 15 U.S.C. 77q(a)(1); 17 C.F.R. 240.10b-5(a) and (c).

3. Aside from his factual challenge, petitioner contends that he "did not violate *either* Section 10(b) *or* Section 17(a)(1) because he did not 'use' or 'employ' a manipulative, deceptive or fraudulent device or scheme." Pet. Br. 48.

To the extent petitioner contends that he did not "use" or "employ" any prohibited form of fraud because he was "merely copying and pasting an email from his boss," that contention is foreclosed by his argument below that he believed the emails' content to be true. Pet. Br. 54; see *Wharf*, 532 U.S. at 594. Indeed, the court of appeals observed that, if petitioner not made such a factual concession, he "might attempt to argue that he cannot be considered to have 'employed' any fraudulent device or artifice, or 'engaged' in any fraudulent or deceitful act." Pet. App. 22. But the court declined to consider that argument—the argument petitioner repeats here—because petitioner "d[id] not challenge" the Commission's factual finding that he was aware of the emails' content. *Ibid.*

To the extent petitioner contends that he did not employ a "manipulative, deceptive or fraudulent device or scheme," his position lacks merit. Pet. Br. 48. As explained above, sending a message designed to induce investment based on false financial information is a quintessential deceptive device. Petitioner contends that this Court's decision in *Chiarella* v. *United States*, 445 U.S. 222 (1980), limits the definition of "deception" to "the making of a misrepresentation" or "an omission or nondisclosure coupled with a duty to speak." Pet. Br. 51. *Chiarella*, however, did not purport to describe the entire universe of prohibited conduct; this Court simply explained that "[w]hen an allegation of fraud is based upon nondisclosure, there can be no fraud absent a duty to speak." 445 U.S. at 235. Because petitioner was not found liable on a nondisclosure theory, his reliance on *Chiarella* is misplaced.

Petitioner's reliance on *Santa Fe Industries, Inc.* v. *Green*, 430 U.S. 462 (1977), is similarly misplaced. There, this Court rejected a theory of liability based on "a breach of fiduciary duty by majority stockholders, without any deception, misrepresentation, or nondisclosure." *Id.* at 476. That holding has no relevance here because petitioner's liability is not based on a fiduciary-breach theory. Likewise, the definition of "manipulation" articulated in *Santa Fe Industries* has no bearing on this case, because petitioner was not charged with "practices, such as wash sales, matched orders, or rigged prices, that are intended to mislead investors by artificially affecting market activity." *Ibid.*; see Pet. Br. 18 ("Here, there is no allegation that Petitioner engaged in manipulative trading practices.").

In short, the plain meaning of the statutory and regulatory provisions "resolves the case." *Central Bank*,

511 U.S. at 177. To the extent petitioner and his amici seek to confine liability to particular "categories" of conduct that are untethered to the relevant text, Pet. Br. 51; see Sec. Indus. & Fin. Markets Ass'n (SIFMA) & Chamber of Commerce Amici Br. 9-11, they seek to add a "gloss to the operative language of the statute quite different from its commonly accepted meaning," *Hochfelder*, 425 U.S. at 199. This Court has repeatedly rejected such efforts in previous cases involving the antifraud provisions. See *ibid.*; see also *Central Bank*, 511 U.S. at 173-174. The Court should similarly apply the text of the relevant provisions here.

B. Petitioner Is Liable For Fraudulent Conduct Under Section 17(a)(1) And Rule 10b-5(a) and (c) Even Though He Did Not "Make" Misstatements Under Rule 10b-5(b)

Petitioner's principal contention (Pet. Br. 26-34) is that he cannot be liable for disseminating deceptive information to investors under Section 17(a)(1) and Rule 10b-5(a) and (c) because he is not liable for "mak[ing]" misstatements under Rule 10b-5(b). That position is misguided. Nothing in the relevant antifraud provisions —or in this Court's precedents interpreting them— precludes the imposition of liability for fraudulent conduct *involving* misstatements under Section 17(a)(1) and Rule 10b-5(a) and (c), even if the defendant is not liable for *making* those misstatements under Rule 10b-5(b). To the contrary, the Commission, lower courts, and this Court have long upheld the imposition of liability under Section 17(a)(1) and Rule 10b-5(a) and (c) for fraudulent conduct that involves misstatements, even in the absence of liability for making misstatements under Rule 10b-5(b).

1. Petitioner relies heavily on this Court's decision in *Janus Capital Group, Inc.* v. *First Derivative Traders*,

564 U.S. 135 (2011), which interpreted Rule 10b-5(b). See *id.* at 141. As relevant here, Rule 10b-5(b) provides that it is unlawful to "make any untrue statement of a material fact" in connection with a securities transaction. 17 C.F.R. 240.10b-5(b). *Janus* involved a private action against an investment-fund adviser that allegedly *drafted* misstatements in prospectuses that were *issued* by a different mutual-fund entity. See 564 U.S. at 147-148. The question before the Court was whether the adviser who had allegedly drafted the misstatements had "made" those misstatements for purposes of Rule 10b-5(b). *Id.* at 141.

The Court concluded that the adviser could not be held liable under Rule 10b-5(b) because the adviser did not "make" the alleged misstatements in the prospectuses. *Janus*, 564 U.S. at 146. Rather, the Court explained, "the maker of a statement" for purposes of Rule 10b-5 "is the person or entity with ultimate authority over the statement." *Id.* at 142. The Court analogized to "the relationship between a speechwriter and a speaker." *Id.* at 143. "Even when a speechwriter drafts a speech, the content is entirely within the control of the person who delivers it. And it is the speaker who takes credit—or blame—for what is ultimately said." *Ibid.* Applying that rule, the Court concluded that the mutual fund had ultimate authority over the statements in the prospectuses, and therefore only the fund—not the investment adviser who had drafted the statements—could be liable for "mak[ing]" misstatements under Rule 10b-5(b). *Id.* at 146-147.

The Court in *Janus* also relied on its prior decisions in *Central Bank* and *Stoneridge Investment Partners, LLC* v. *Scientific-Atlanta, Inc.*, 552 U.S. 148 (2008). See *Janus*, 564 U.S. at 142-146. In both of those cases

(discussed further below in Section C), the Court declined to extend primary liability to secondary actors who did not directly deceive investors, but rather played a behind-the-scenes role in facilitating the fraud. See *Stoneridge*, 552 U.S. at 152-153 (declining to extend liability to customers and suppliers who facilitated the primary actor's fraud); *Central Bank*, 511 U.S. at 167-168 (declining to extend liability to bank that played supporting role in fraud). The *Janus* Court concluded that there was "no reason to treat participating in the drafting of a false statement differently from engaging in deceptive transactions, when each is merely an undisclosed act preceding the decision of an independent entity to make a public statement." 564 U.S. at 145.

Applying *Janus*, the court of appeals here concluded that petitioner did not "mak[e]" the false statements in the emails sent to investors for purposes of Rule 10b-5(b) because Gregg Lorenzo, rather than petitioner, "retained ultimate authority" over the emails' contents. Pet. App. 16-17; see *id.* at 19 ("Under the Supreme Court's decision in *Janus*," petitioner "cannot be considered to have been 'the maker' of the statements in question for purposes of Rule 10b-5(b).").

Petitioner seeks to extend the finding that he did not "make" misstatements for purposes of Rule 10b-5(b) into a conclusion that he did not violate *any* provision of Rule 10b-5 or Section 17(a)(1). Pet. Br. 26-28. The court of appeals correctly rejected that attempted bootstrapping, see Pet. App. 22-27, and this Court should too. The *Janus* Court had no occasion to address, and did not address, the scope of Rule 10b-5(a), Rule 10b-5(c), or Section 17(a). The district court in the underlying litigation dismissed claims brought under Rule 10b-5(a) and (c), and the court of appeals did not address

that holding. See *In re Mutual Funds Inv. Litig.*, 487 F. Supp. 2d 618, 622 (D. Md. 2007), rev'd, 566 F.3d 111 (4th Cir. 2009), rev'd, 564 U.S. 135 (2011). In this Court, the *Janus* petitioners emphasized that the only issue presented for review involved the scope of Rule 10b-5(b). See Pet. Br. at 40 n.8, *Janus*, *supra* (No. 09-525). The *Janus* petitioners' counsel stated at oral argument that "[t]here is no 10b-5(a) claim in this case. This is only a 10b-5(b) 'making' claim." 12/7/10 Tr. at 5, *Janus*, *supra* (No. 09-525). And this Court's opinion did not even cite, let alone interpret, Rule 10b-5(a), Rule 10b-5(c), or Section 17(a)(1).

The *Janus* Court's construction of the term "make" in Rule 10b-5(b), moreover, has no necessary implications for the scope of other antifraud provisions that do not use that word. See *U.S. SEC* v. *Big Apple Consulting USA, Inc.*, 783 F.3d 786, 797 (11th Cir. 2015) (stating that, because *Janus*'s reasoning is based on the text of Rule 10b-5(b), its holding "does not apply" beyond that subsection) (citation omitted); *SEC* v. *Monterosso*, 756 F.3d 1326, 1334 (11th Cir. 2014) (per curiam) (similar); *SEC* v. *Pentagon Capital Mgmt. PLC*, 725 F.3d 279, 287 (2d Cir. 2013) (similar). To the contrary, extending *Janus*'s construction of the term "make" in Rule 10b-5(b) to provisions that do not include that term would contravene the presumption that "differences in language * * * convey differences in meaning." *Henson* v. *Santander Consumer USA Inc.*, 137 S. Ct. 1718, 1723 (2017). Imposing this Court's interpretation of Rule 10b-5(b) on other provisions would be especially inappropriate in light of this Court's decisions emphasizing that the subparts of Section 17(a) and Rule 10b-5

are each "meant to cover additional kinds of illegalities." *Naftalin*, 441 U.S. at 774; see *Affiliated Ute*, 406 U.S. at 152-153.

As explained above, petitioner's dissemination of messages containing false financial information constitutes a paradigmatic "device, scheme, or artifice to defraud" under Section 17(a)(1) and Rule 10b-5(a) and an "act, practice, or course of business which operates" as a fraud under Rule 10b-5(c). 15 U.S.C. 77q(a)(1); 17 C.F.R. 240.10b-5(a) and (c). That remains true even though petitioner did not "make" a misstatement for purposes of Rule 10b-5(b). Unlike the defendants in *Janus* and in earlier similar cases, moreover, petitioner did not play an "undisclosed," behind-the-scenes role as a preliminary actor. Pet. App. 24. He sent the messages "directly" to the prospective investors "from his account and under his name." *Ibid.* Imposing liability on petitioner under those circumstances is fully consistent with *Janus*.

2. Imposing liability on petitioner for fraudulent conduct even though he did not make a misstatement is also consistent with deeply rooted understandings of securities fraud as interpreted by the Commission, lower courts, and this Court.

When interpreting the antifraud provisions of the federal securities laws, this Court has looked to the common law while "eschew[ing] rigid common-law barriers." *Bateman Eichler, Hill Richards, Inc.* v. *Berner*, 472 U.S. 299, 310 (1985). That approach reflects the recognition that "an important purpose of the federal securities statutes was to rectify perceived deficiencies in the available common-law protections by establishing higher standards of conduct in the securities industry." *Herman & MacLean* v. *Huddleston*, 459 U.S. 375, 389

(1983). It therefore "is well known that the federal securities laws provide broader fraud protection than the common law, having been enacted in response to the common law's perceived failure at stamping out fraud in the securities markets." *MBIA Ins. Corp.* v. *Royal Indem. Co.*, 426 F.3d 204, 218 (3d Cir. 2005) (Alito, J.). *A fortiori*, if petitioner's conduct would have exposed him to liability under the common law, it is covered by the federal antifraud provisions.

Petitioner's willful dissemination of material misstatements to potential investors would have constituted actionable fraud at common law, even though the misstatements that petitioner disseminated were made by Gregg Lorenzo. In particular, under the "common law offense of obtaining property by false pretenses," a defendant who engaged in deceitful or fraudulent conduct could be held liable even if he did not personally make the false representation that defrauded the plaintiff. *In re Dennis J. Malouf*, Securities Act Release No. 10115, at 10, 2016 WL 4035575 (July 27, 2016) (*Malouf*, Release No. 10115), corrected by Securities Act Release No. 10207, 2016 WL 4761084 (Sept. 13, 2016); see 1 Melville M. Bigelow, *A Treatise on the Law of Fraud on its Civil Side* 247 (1888) (explaining that liability for fraud exists "where a man has conspired with others to cheat and defraud the plaintiff in the sale of certain property, by fraudulent concealments and misrepresentations * * * even where he has not himself made any of the misrepresentations").[2]

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[2] See also, *e.g.*, *Zuckerman* v. *Cochran*, 158 So. 324, 326 (Ala. 1934) (plaintiff stated a claim in an action for deceit in the purchase of real estate where the defendant had participated in "a fraudulent scheme" even though the plaintiff was duped by misrepresentations

Early practice under the federal securities-fraud laws supports the view that cases involving misstatements may be brought under Section 17(a)(1) and Rule 10b-5(a) or (c). During the period between Section 17(a)'s enactment and Rule 10b-5's promulgation, the Commission did not interpret the statute's subsections as mutually exclusive. See, *e.g.*, *In re Arthur Hays & Co.*, 5 S.E.C. 271, 1939 WL 36375 (July 10, 1939) (finding violations of Sections 17(a)(2) and (3) based on the same misconduct of fraudulently inducing a party to purchase stock); *In re Foreman & Co., Inc.*, 3 S.E.C. 132, 1938 WL 34031 (Feb. 2, 1938) (not distinguishing between Section 17(a)'s subsections). After adopting Rule 10b-5, the Commission did not typically distinguish between subsections in finding violations of the Rule, see, *e.g.*, *In re Ward La France Truck Corp.*, 13 S.E.C. 373, 1943 WL 29807 (May 20, 1943), and when it did, the Commission did not view the subsections as mutually exclusive, see also *In re R. D. Bayly & Co. 727 W. 7th St. Los Angeles*, 19 S.E.C. 773, 1945 WL 26109 (July 14, 1945) (finding violations of provisions that would be renumbered as Rule 10b-5(b) and (c), based on the same material misrepresentations and misleading omissions).

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of a different participant in the scheme); *Cheney* v. *Powell*, 15 S.E. 750, 751 (Ga. 1892) ("One who makes willfully false representations, to be fraudulently used by another as an inducement to a third person to enter into a contract with the party repeating them, is as much guilty of a deceit as the latter, and is equally liable to the party deceived."); *Bank of Commerce & Trust Co.* v. *Schooner*, 160 N.E. 790, 792 (Mass. 1928) (imposing liability on a defendant who had participated in a "scheme to defraud" by engaging in deceptive conduct that led to a plaintiff being induced to lend "large sums of money upon worthless securities," even though the representations to the plaintiff were made by another).

That does not mean the text of the provisions did not matter, but instead that the provisions' coverage overlapped. In a seminal early decision, the Commission described the provisions in Rule 10b-5 and Section 17(a) as "mutually supporting rather than mutually exclusive." *In re Cady, Roberts & Co.*, 40 S.E.C. 907, 913, 1961 WL 60638 (Nov. 8, 1961); see, *e.g.*, *Chiarella*, 445 U.S. at 228 (relying on *In re Cady, Roberts*). Early judicial interpretations reflected the same approach.[3]

This Court's precedents reinforce the conclusion that liability for frauds involving misstatements can be imposed under provisions other than Rule 10b-5(b). In *Affiliated Ute*, the Court held that two defendants who had "devised a plan and induced" certain sellers of stock "to dispose of their shares" without knowing material facts about the value of the stock had engaged in "a 'course of business' or a 'device, scheme, or artifice' that operated as a fraud" on others. 406 U.S. at 153 (citation omitted). The Court reached that conclusion even

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[3] See *Speed* v. *Transamerica Corp.*, 99 F. Supp. 808, 829 (D. Del. 1951) (breach of duty of disclosure "can be viewed as a violation of all three subparagraphs"); *Kardon* v. *National Gypsum Co.*, 73 F. Supp. 798, 800 (E.D. Pa. 1947); (three subsections violated through failure "to disclose a fact coming to [directors' and officers'] knowledge by reason of their position, which would materially affect the judgment of the other party to the transaction"); *Charles Hughes & Co.* v. *SEC*, 139 F.2d 434, 436 (2d Cir. 1943) ("Although the Commission has neglected to make any finding" addressing whether petitioner made "false statements of material fact," "we need not remand for a specific finding resolving this conflict, for we feel that petitioner's mark-up policy operated as a fraud and deceit upon the purchasers, as well as constituting an omission to state a material fact" under Section 17(a).), cert. denied, 321 U.S. 786 (1944).

though the "defendants may have made no positive representation or recommendation" to some of the plaintiffs, and even though the fraudulent scheme also involved "a misstatement of a material fact" made by others regarding "the prevailing market price of the * * * shares" of stock at issue. *Id.* at 152-153. The Court stated that, while Rule 10b-5(b) "specifies the making of an untrue statement of a material fact and the omission to state a material fact," the "first and third subparagraphs" of Rule 10b-5 "are not so restricted." *Id.* at 150-153.

Similarly in *Chadbourne & Parke LLP* v. *Troice*, 134 S. Ct. 1058 (2014), the Court recently indicated that false statements may form the basis for liability under Rule 10b-5(a). The Court described Rule 10b-5 as "forbid[ding] the use of any 'device, scheme, or artifice to defraud' (*including* the making of 'any untrue statement of a material fact' or any similar 'omi[ssion]') 'in connection with the purchase or sale of any security.'" *Id.* at 1063 (emphasis added; citation omitted; brackets in original). The Court thus characterized the making of a false statement to obtain money or property as a type of "device, scheme, or artifice to defraud," not as a separate category of conduct.

Those decisions reinforce the conclusion that claims involving false statements may proceed under Rule 10b-5(a) and (c) (as well as Section 17(a)(1)). Petitioner's theory—that fraud claims in any way involving false statements can proceed only under Rule 10b-5(b) (or Section 17(a)(2)) and only against the maker of the misstatements—would require a radical departure from those principles and decisions.

C. Imposing Liability For Petitioner's Active Deception Preserves The Distinction Between Primary And Secondary Liability

Petitioner further contends (Pet. Br. 35-44) that imposing liability for his conduct under Section 17(a)(1) and Rule 10b-5(a) and (c) would eliminate the distinction between primary and secondary liability that this Court emphasized in *Central Bank* and *Stoneridge*. That argument lacks merit. Because petitioner's *own* conduct in disseminating false financial information to investors constituted a "device, scheme, or artifice to defraud" and an "act, practice, or course of business which operates" as a fraud, he is *primarily* liable for violating Section 17(a)(1) and Rule 10b-5(a) and (c). 15 U.S.C. 77q(a)(1); 17 C.F.R. 240.10b-5(a) and (c). That conclusion does not affect the balance between primary and secondary liability announced in *Central Bank* and *Stoneridge*.

1. The question in *Central Bank* was "whether private civil liability under § 10(b) extends as well to those who do not engage in the manipulative or deceptive practice, but who aid and abet the violation." 511 U.S. at 167. The Court declined to extend aiding-and-abetting liability to those circumstances. The Court emphasized the importance of the reliance element in private Rule 10b-5 suits, stating that if it "allow[ed] the aiding and abetting action proposed in this case, the defendant could be liable without any showing that the plaintiff relied upon the aider and abettor's statements or actions." *Id.* at 180. The Court clarified, however, that "[a]ny person or entity" who violates Rule 10b-5 "may be liable as a *primary* violator under 10b-5, assuming all of the requirements for primary liability under Rule 10b-5 are met." *Id.* at 191 (emphasis added and omitted).

The decision below and the SEC's general approach to cases of this nature are consistent with the *Central Bank* framework. Under the SEC's view, defendants whose conduct violates Section 17(a) or Rule 10b-5 are primarily liable, while "[d]efendants who merely obtain or transmit legitimate documents knowing that they would later be falsified in order to misstate a company's financial condition would not be primarily liable under Rule 10b-5(a) and (c), but could be" secondarily liable "for aiding and abetting." *Malouf*, Release No. 10115, at 16 n.61. Those defendants would be aiders and abettors "provid[ing] substantial assistance to another person" who was violating an antifraud provision, and therefore would be subject to an enforcement action by the Commission, 15 U.S.C. 78t(e), but they would not be employing a device, scheme, or artifice to defraud or engaging in an act, practice, or course of business which operates or would operate as a fraud or deceit. They consequently could not be held primarily liable for violating Section 17(a)(1) or Rule 10b-5(a) or (c).

"Similarly, defendants who engage in legitimate, rather than sham, transactions generally would *not* be primarily liable under Rule 10b-5(a) and (c), even if they knew or intended that another party would manipulate the transaction to effectuate a fraud." *Malouf*, Release No. 10115, at 16 n.61 (emphasis added; citation and internal quotation marks omitted). And defendants "who have no fiduciary duty of disclosure but who are aware of a fraud and have the potential to benefit from it but take no action to stop it also would be aiders and abettors of a Rule 10b-5 violation rather than primary violators themselves." *Ibid.* In those scenarios, "because their own conduct was not deceptive" but the defend-

ants knowingly provided substantial assistance to another person committing fraud, "the defendants are aiders and abettors rather than primary violators." *Ibid.*

The decision below does not render aiding-and-abetting liability "almost indistinguishable" from primary liability, nor does it create a "backdoor" route to imposing primary liability on those who do "no more than provide substantial assistance to another person." Pet. Br. 37, 44-45. Petitioner was found primarily liable for his *own fraudulent conduct*—his "active 'role in producing and sending'" material misstatements with deceptive intent, and for thereby "employing a deceptive 'device,' 'act,' or 'artifice to defraud.'" Pet. App. 21 (citation omitted). He "effectively vouched for the emails' contents and put his reputation on the line by listing his personal phone number and inviting the recipients to 'call with any questions.'" *Id.* at 24 (citation omitted). Because petitioner himself engaged in deceptive acts, and his conduct satisfied "all of the requirements for primary liability" under the antifraud provisions, he is a primary rather than a secondary violator. *Central Bank*, 511 U.S. at 191 (emphasis omitted).

2. Imposing liability on petitioner for his own fraudulent conduct is equally consistent with *Stoneridge*. The Court in *Stoneridge* addressed whether, in a private action brought by investors under Section 10(b), customers and suppliers could be liable for "agree[ing] to arrangements that allowed the investors' company to mislead its auditor and issue a misleading financial statement affecting the stock price." 552 U.S. at 152-153. The Court emphasized that "[c]onduct itself can be deceptive," and a "course of conduct" may "include[] both oral and written statements." *Id.* at 158. The Court

held, however, that the private plaintiffs could not prevail because the customers' and suppliers' "acts or statements were not relied upon by the investors." *Id.* at 159.

That basis for rejecting liability is inapposite here. The Commission is not required to prove reliance in its own enforcement actions. See *SEC* v. *Morgan Keegan & Co.*, 678 F.3d 1233, 1244 (11th Cir. 2012) (per curiam) (collecting authorities). And petitioner's conduct was clearly intended to engender reliance on the part of the investors who received the emails. Unlike the defendants in *Stoneridge*, who did not interact directly with the investors and whose actions "did not have the requisite proximate relation to the investors' harm," 552 U.S. at 158-159, petitioner himself sent the false emails to investors and placed his imprimatur on their contents by telling investors to direct any questions to him. Imposing liability for petitioner's own "course of conduct" is fully consistent with *Stoneridge*. *Id.* at 158.

D. No Canon Of Construction Supports Departing From The Text, History, And Purpose Of The Charged Antifraud Provisions

Petitioner briefly contends (Pet. Br. 29) that subjecting him to liability under Section 17(a)(1) and Rule 10b-5(a) and (c), but not under Rule 10b-5(b), would violate the canon against redundancy, because "all claims for false statements could be brought as fraudulent scheme claims, and, vice-versa." That position is misguided. As the Commission has explained, it "would be arbitrary to read th[e] terms" of Section 17(a)(1) and Rule 10b-5(a) and (c) "as excluding the making, drafting, or devising of a misstatement or omission" simply because Rule 10b-5(b) specifically penalizes the makers of misstatements. *Malouf*, Release No. 10115, at 15.

1. It is "hardly a novel proposition" that different provisions of the securities laws "'prohibit some of the same conduct.'" *Huddleston*, 459 U.S. at 383 (citation omitted). Some measure of overlap was an "understandable" result of the fact that "[t]he Securities Act of 1933 was the first experiment in federal regulation of the securities industry." *SEC* v. *Capital Gains Research Bureau*, 375 U.S. 180, 197-199 (1963). Section 17(a) was thus intentionally crafted to "include both a general proscription against fraudulent and deceptive practices and, out of an abundance of caution, a specific proscription against" nondisclosure under Section 17(a)(2), even though "a specific proscription against nondisclosure" was "surplusage." *Id.* at 198-199. "Each succeeding prohibition" of Section 17(a) "is meant to cover additional kinds of illegalities—not to narrow the reach of the prior sections." *Naftalin*, 441 U.S. at 774.

This Court and lower courts have accordingly read the subsections of Section 17(a) as mutually reinforcing rather than mutually exclusive. See *Naftalin*, 441 U.S. at 774; *United States* v. *Yeaman*, 194 F.3d 442, 453 (3d Cir. 1999) ("While each category [of Section 17(a)] has its own parameters, they are largely overlapping categories and all fall within the traditional understanding of the concept of fraud. Most conduct that falls within one is likely to satisfy another as well.") (citation omitted); cf. *United States* v. *Swanson*, 360 F.3d 1155, 1162 (10th Cir. 2004) ("Although largely overlapping, a scheme to defraud, and a scheme to obtain money by means of false or fraudulent pretenses, representations, or promises, are separate offenses." (quoting *United States* v. *Cronic*, 900 F.2d 1511, 1513 (10th Cir. 1990) (brackets omitted)). The Commission adopted the same

approach in drafting Rule 10b-5, which borrows much of its language from Section 17(a). See pp. 15-16, *supra*.

If the Commission had intended to avoid any redundancy between Rule 10b-5 and Section 17(a), it would not have incorporated substantial portions of the statute's language into the text of the Rule. Nor would it have applied the rule to "the purchase or sale of any security," 17 C.F.R. 240.10b-5, when Section 17(a) already applied to "the offer or sale of any securities," 15 U.S.C. 77q(a). The Commission's concern with stamping out all forms of fraud, rather than avoiding any possible redundancies, is thus apparent from the text of Rule 10b-5 itself. Cf. *Ki Se Lee* v. *Ashcroft*, 368 F.3d 218, 227 (3d Cir. 2004) (Alito, J., dissenting) ("[E]ven if the drafters [of 26 U.S.C. 7201, the federal tax-evasion statute] could not think of an evasion case that did not involve fraudulent or deceitful conduct, the drafters might not have trusted their ability to anticipate every possible variety of evasion case and might have added" a potentially redundant subsection "just to be sure that no evasion case fell outside the definition.").

In any event, although the Commission's longstanding view is that Section 17(a)(1) and Rule 10b-5(a) and (c) do not categorically "exclud[e] the making, drafting, or devising of a misstatement or omission," *Malouf*, Release No. 10115, at 15 (emphasis omitted), the court of appeals held that petitioner did not "make" the false statements at issue here, Pet. App. 15. This case therefore does not directly present the question whether a person who "makes" a misstatement, and therefore is potentially liable under Rule 10b-5(b), may be liable under Rule 10b-5(a) or (c) and/or Section 17(a) as well. Instead, the Court need only decide whether conduct otherwise encompassed by those provisions—here, the

knowing dissemination of false statements to obtain money from investors—is categorically excluded from primary liability under all of those provisions merely because the false statements were "made" by another.

2. Petitioner likewise derives no benefit from the rule of lenity. The rule of lenity "only applies if, after considering text, structure, history, and purpose, there remains a 'grievous ambiguity or uncertainty in the statute,'" *Barber* v. *Thomas*, 560 U.S. 474, 488 (2010) (quoting *Muscarello* v. *United States*, 524 U.S. 125, 139 (1998)), such that "the equipoise of competing reasons cannot otherwise be resolved," *Johnson* v. *United States*, 529 U.S. 694, 713 n.13 (2000). No such circumstance exists here. As explained above, relevant text, structure, history, and purpose all demonstrate that Congress and the Commission intended the antifraud provisions at issue here to be mutually reinforcing rather than mutually exclusive. See p. 35, *supra*. Thus, even if the Court finds the statute and regulation not to be "crystalline," it can still "make far more than 'a guess as to what Congress'" and the Commission intended, which prevents the rule of lenity from "apply[ing] in [petitioner's] favor." *DePierre* v. *United States*, 564 U.S. 70, 88 (2011) (citation omitted).

E. Petitioner's Policy Arguments Provide No Sound Basis For Reversing The Court Of Appeals' Judgment

Petitioner contends (Br. 17-18, 28) that the decision below will allow meritless private suits against defendants who would otherwise be secondary actors insulated from liability in private securities-fraud suits. Under the court of appeals' decision, however, a defendant will not be primarily liable under the antifraud provisions at issue here unless his own conduct is deceptive. A defendant will be liable only if "each of the elements or

preconditions for liability" under Rule 10b-5 has been satisfied. *Stoneridge*, 552 U.S. at 158. And unlike the Commission, private plaintiffs cannot prevail unless they demonstrate reliance on the defendant's own misconduct, see *Morgan Keegan* 678 F.3d at 1244 (collecting authorities), as well as economic loss and loss causation, see *Dura Pharms., Inc.* v. *Broudo*, 544 U.S. 336, 341-342 (2005).

The PSLRA affords additional protections to defendants in private securities-fraud suits. The PSLRA (which does not apply to actions brought by the Commission) requires that, "if an allegation regarding the statement or omission is made on information and belief, the complaint shall state with particularity all facts on which that belief is formed." 15 U.S.C. 78u-4(b)(1). The plain text of the PSLRA thus encompasses any "statement or omission" that is alleged to have played a role in a violation of the securities laws. It does not distinguish between statements or omissions that are prohibited by Rule 10b-5(b) and statements or omissions that constitute (or are used to carry out) a deceptive device, act, or artifice to defraud under Rule 10b-5(a) or (c). *Ibid.* There is accordingly no need to exclude false-statement claims from Rule 10b-5(a) and (c) to prevent evasion of the PSLRA.

In addition to establishing those heightened pleading requirements, the PSLRA sets "limits on damages and attorney's fees, a 'safe harbor' for certain kinds of statements, restrictions on the selection of lead plaintiffs in securities class actions, sanctions for frivolous litigation, and stays of discovery pending motions to dismiss." *Halliburton Co.* v. *Erica P. John Fund, Inc.*, 134 S. Ct. 2398, 2413 (2014). "Congress later fortified

the PSLRA by enacting the Securities Litigation Uniform Standards Act of 1998, 112 Stat. 3227, which curtailed plaintiffs' ability to evade the PSLRA's limitations on federal securities-fraud litigation by bringing class-action suits under state rather than federal law." *Amgen Inc.* v. *Connecticut Ret. Plans & Trust Funds*, 568 U.S. 455, 476 (2013). Those additional requirements provide further assurance that interpreting Rule 10b-5 according to its terms will not encourage meritless private suits.

Adoption of petitioner's approach would create a significant loophole in the federal securities laws. The conduct in which petitioner engaged—using false statements to obtain money from investors —is a paradigmatic form of fraud. Under petitioner's theory, however, knowing dissemination of such false statements could not form the basis for primary liability if the false statements were "made" by a third party. And if the maker of the statement acted without scienter, neither the maker nor the disseminator could be subjected to either primary or secondary liability. See 15 U.S.C. 78t(e) (providing that, in specified circumstances, a person who aids or abets a securities-law violation "shall be deemed to be in violation of such provision to the same extent as the person to whom such assistance is provided"). That approach would subvert the efforts of Congress and the Commission to fashion a comprehensive scheme that outlaws all forms of securities fraud.

Petitioner argues (Pet. Br. 57) that "any decision to expand liability to new classes of defendants should be left to Congress." But the conduct in which petitioner was found to have engaged has long been treated as actionably fraudulent, both under the federal securities laws and under their common-law antecedents. A clear

statement by this Court reiterating that the antifraud provisions at issue here should be interpreted according to their plain text would promote rather than undermine certainty and predictability.

CONCLUSION

The judgment of the court of appeals should be affirmed.

Respectfully submitted.

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APPENDIX

1. 15 U.S.C. 77q(a) (2006) provides:

Fraudulent interstate transactions

(a) Use of interstate commerce for purpose of fraud or deceit

It shall be unlawful for any person in the offer or sale of any securities or any security-based swap agreement (as defined in section 206B of the Gramm-Leach-Bliley Act) by the use of any means or instruments of transportation or communication in interstate commerce or by use of the mails, directly or indirectly—

(1) to employ any device, scheme, or artifice to defraud, or

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

2. 15 U.S.C. 78j (2006) provides in pertinent part:

Manipulative and deceptive devices

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—

* * * * *

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, or any securities-based swap agreement (as defined in section 206B of the Gramm-Leach-Bliley Act), any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

* * * * *

3. 15 U.S.C. 78u-4(b)(1) provides:

Private securities litigation

(b) Requirements for securities fraud actions

(1) Misleading statements and omissions

In any private action arising under this chapter in which the plaintiff alleges that the defendant—

(A) made an untrue statement of a material fact; or

(B) omitted to state a material fact necessary in order to make the statements made, in the light of the circumstances in which they were made, not misleading;

the complaint shall specify each statement alleged to have been misleading, the reason or reasons why the statement is misleading, and, if an allegation regarding the statement or omission is made on information and belief, the complaint shall state with particularity all facts on which that belief is formed

4. 17 C.F.R. 240.10b-5 provides:

Employment of manipulative and deceptive devices.

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.

No. 17-1077

In the Supreme Court of the United States

FRANCIS V. LORENZO,
Petitioner,

v.

SECURITIES AND EXCHANGE COMMISSION,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

REPLY BRIEF FOR PETITIONER

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STATEMENT PURSUANT TO RULE 29.6

There are no amendments to Petitioner's corporate disclosure statement as set forth in the Petition for a Writ of Certiorari.

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INTRODUCTION

In *Janus Capital Group, Inc. v. First Derivative Traders*, 564 U.S. 135 (2011) this Court held that one who does not make a misstatement cannot be held primarily liable for that misstatement under Section 10(b) of the Securities Exchange Act of 1934 (15 U.S.C. § 78j) and Rule 10b-5 (17 CFR 240.10b-5). While the SEC argues that the *Janus* holding should be limited to Rule 10b-5(b), the language of the *Janus* decision and the Court's reliance on its earlier decisions interpreting Section 10(b) do not support limiting *Janus* to only subsection (b). The SEC does not provide a supportable rationale for such a narrow reading of *Janus*. Moreover, allowing inadequate misstatement claims to simply be plead under Rules 10b-5(a), 10b-5(c) and 17(a)(1) of the Securities Act of 1933 (15 U.S.C. § 77q(a)(1)) would render *Janus* and Rule 10b-5(b) meaningless.

The SEC's brief also fails to address Petitioner's argument that Petitioner's conduct falls outside of the text of Sections 10(b) of the Exchange Act and 17(a)(1) of the Securities Act. Instead, the SEC's arguments in support of primary liability for Petitioner rest almost exclusively on the text of Rules 10b-5(a) and 10b-5(c). However, an administrative rule cannot go further than the statute on which it is based in proscribing conduct. The SEC's opposition brief also fails to cite a single precedent under any legal rule holding a defendant primarily liable for merely disseminating a statement made by another.

The SEC's argument that Petitioner took a different factual position in the D.C. Circuit than he did in this Court concerning his belief in the accuracy of the

statements in the emails is not only incorrect but it is barred by Supreme Court Rule 15.2, which requires the Respondent's brief in opposition to address any perceived misstatement of fact or law in the petition that bears on what issues properly would be before the Court if certiorari were granted. Moreover, Petitioner has not challenged the D.C. Circuit's holding on scienter and the SEC's arguments regarding Petitioner's purported different factual positions do not relate in any way to the question presented in this appeal.

The Petitioner's merits brief also demonstrated that the D.C. Circuit's decision effectively erased the distinction between primary and secondary liability under the securities laws. The SEC argues that the D.C. Circuit's decision preserves this distinction because Petitioner's own conduct makes him a primary violator of the securities laws. However, the only conduct Petitioner was found to have engaged in was producing and sending the emails in question. It was this ministerial conduct alone that the D.C. Circuit relied on when holding that Petitioner's dissemination of the statements in the emails -- of which he was not the maker -- constituted employing a deceptive 'device,' 'act,' or 'artifice to defraud.' The D.C. Circuit's low threshold for primary liability gives virtually no weight to Congress's well thought out distinction between primary and secondary liability and effectively revives private claims for aiding and abetting liability in contravention of *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164 (1994).

ARGUMENT

I. The SEC's Argument that a Defendant Who Did Not Make a Misstatement Could Still be Liable Under Rules 10b-5(a) and (c) and Section 17(a)(1) Undercuts the Holding in *Janus*

Petitioner's merits brief established that the D.C. Circuit erred when it held that Petitioner could be held primarily liable for violating Section 10(b), Rules 10b-5(a) and (c) and Section 17(a)(1) even though Petitioner was not the "maker" of the misstatements under the standards set forth in *Janus*.[1] Petitioner's brief also established that the D.C. Circuit erred when it held that Petitioner's ministerial role in sending the emails could constitute employing a deceptive 'device,' 'act,' or 'artifice to defraud' for purposes of primary liability under Section 10(b), Rule 10b-5(a) and (c), and Section17(a)(1). Once the D.C. Circuit found that Lorenzo was not the maker of the misstatements – and that Lorenzo did no more than produce[2] and send emails containing statements made by another – its inquiry should have ended.

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[1] *Amicus* North American Securities Administrators Association argues that the D.C. Circuit incorrectly held Petitioner did not "make" the statement under Rule 10b-5(b) within the meaning of *Janus* (NASAA Br. 18-25), however the SEC has not contested this holding and the argument is outside the question presented in this appeal.

[2] The D.C. Circuit did not cite any specific conduct that lead it to conclude Petitioner "produced" the emails.

In response to Petitioner's arguments that *Janus* forecloses liability on Rule 10b-5(a), 10b-5(c) and Section 17(a)(1) the SEC offers an extremely cramped reading of *Janus* and argues that the "*Janus* Court had no occasion to address, and did not address, the scope of Rule 10b-5(a), Rule 10b-5(c), or Section 17(a)" and that the "*Janus* Court's construction of the term "make" in Rule 10b-5(b), moreover, has no necessary implications for the scope of other antifraud provisions that do not use that word." (Resp. Br. 25)

It would be a mistake to adopt the SEC's argument and read *Janus* as a decision addressed solely to misstatements liability under Rule 10b-5(b), and not to misstatements liability generally under Section 10(b), Rule 10b-5 and Section 17(a)(1) as a whole. In fact, the *Janus* Court was careful to note that the "rule" it announced "follow[ed] from" its decisions interpreting Section 10(b) and Rule 10b-5 such as *Central Bank*, 511 U.S. at 143, and described that "rule" as applying "for purposes of Rule 10b-5" – not just subsection (b) of Rule 10b-5. *Janus*, 564 U.S. at 142, 148 & n.12.

The D.C. Circuit's decision also improperly blurred the statutory and regulatory distinction between fraudulent misstatements on one hand and fraudulent conduct on the other. Unlike Rule 10b-5(b), neither Rule 10b-5(a) nor 10b-5(c) uses the word "statement." Instead, subsection (a) refers to "any device, scheme or artifice" and subsection (c) refers to "any act, practice, or course of business." The text in subsections (a) and (c) do not address speaking, writing, or otherwise communicating, and are not synonymous with making a "statement." This is particularly true when the text of subsections (a) and (c) is compared with the text of

subsection (b) and its express focus on "statement[s]." Given this structure, subsections (a) and (c) are best read to be referring to conduct other than statements. Indeed, if subsections (a) and (c) embody all misstatement cases, then subsection (b) has no purpose or meaning at all -- a result at odds with the established principle that courts should not read "text in a way that makes part of it redundant." *See Corley v. United States*, 556 U.S. 303, 314 (2009); *Nat'l Ass'n of Home Builders v. Defs. of Wildlife*, 551 U.S. 644, 669 (2007).

A. The SEC Proposes a Very Limited Reading of *Janus* that Makes the Decision Meaningless

Adopting the SEC's argument would permit every inadequate misstatement claim to be repackaged as a claim under Rules 10b-(a) and (c) and 17(a)(1) for employing a deceptive 'device,' 'act,' or 'artifice to defraud.' If the SEC's limited reading of *Janus* is accepted, the decision would become a nullity. In fact, the SEC's brief never suggests any situation to which *Janus* would apply if the SEC's reading of Rule 10b-5 prevails. The SEC's brief also does not suggest any convincing rationale as to why the holding in *Janus* should not be extended to Rule 10b-5(a), Rule 10b-5(c) and Section 17(a)(1).

Moreover, this is not a case of "some measure of overlap" between the subsections as the SEC argues (Resp. Br. 35) -- this is a wholesale erasure of one of the subsections and the elimination of the important distinction between fraudulent statements and fraudulent conduct. This Court has specifically cautioned "against reading a text in a way that makes

part of it redundant" *Nat'l Ass'n Home Builders v. Defenders of Wildlife*, 551 U.S. 644, 669 (2007). In offering this reading of *Janus* the SEC ignores crucial elements of the decision including the *Janus* Court's reading of Section 10(b) and its reliance on *Stoneridge Investment Partners, LLC v. Scientific-Atlanta*, 552 U.S. 148 (2008), and *Central Bank*, neither of which turned on the text of Rule 10b-5, but rather rested on concerns about inappropriately expanding primary liability in a way that Congress never intended.

B. The SEC Misconstrues The Common Law Backdrop For Section 10(b)

The SEC's brief asserts that "the Commission, lower courts, and this Court have long upheld the imposition of liability under Section 17(a)(1) and Rule 10b-5(a) and (c) for fraudulent conduct that involves misstatements, even in the absence of liability for making misstatements under Rule 10b-5(b)" (Resp. Br. 13), yet the SEC does not cite a single case where a person has been held primarily liable for disseminating misstatements made by another. The SEC's reliance on common law in arguing that Petitioner should be held primarily liable is also misplaced.

The SEC mistakenly argues that the federal securities laws provide broader fraud protection than the common law and, *a fortiori*, if Petitioner's conduct would have exposed him to liability under the common law, the conduct would also be covered by the federal antifraud provisions. (Resp. Br. 27) But this has never been the law, and this Court explicitly rejected this argument in *Stoneridge* when it stated "Section 10(b) does not incorporate common-law fraud into federal

law." *Stoneridge*, 552 U.S. at 162 (collecting cases).[3] Indeed, in a case cited by the SEC, then-Judge Alito found that Section 10(b) cases do not "provide reliable guidance" as to what the common law would hold. *MBIA Ins. Corp. v. Royal Indem. Co.*, 426 F.3d 204, 218 (3d Cir. 2005) (Alito, J.). Thus, while the SEC is correct that the securities laws go beyond the common law in some instances, and while the private Section 10(b) cause of action draws on some common law doctrines, the SEC's reliance on common law does not answer the question before the Court.

In fact, the common law authorities cited by the SEC only underline the fact that the common law would not treat the SEC's theory as one of primary fraud. All of the precedents cited by the SEC involved common law conspiracy claims. *See Zuckerman v. Cochran*, 158 So. 324, 325 (Ala. 1934) ("statements were made in accord with the fraudulent and wrongful conspiracy or agreement"); *Bank of Commerce & Trust Co. v. Schooner*, 160 N.E. 790, 791 (Mass. 1928) ("the

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[3] The SEC reached the opposite conclusion in *In re Dennis J. Malouf*, Securities Act Release No. 10115, at 10, 2016 WL 4035575 at *6 n. 22 (July 27, 2016) (*Malouf*, Release No. 10115), corrected by Securities Act Release No. 10207, 2016 WL 4761084 (Sept. 13, 2016) but it did so entirely on the basis of Circuit decisions from the 1970s without citing or discussing *Stoneridge*. *Malouf* elsewhere relies on district court cases predating *Stoneridge* for propositions explicitly rejected by this Court in *Stoneridge*. *See Malouf*, 2016 WL 4035575, at *8 nn. 44 & 50. This is precisely the sort of antagonistic treatment of this Court's precedents that then-Judge Kavanaugh criticized in his dissent below. *See* App. 47 n.4 (citing Andrew N. Vollmer, *SEC Revanchism and the Expansion of Primary Liability Under Section 17(a) and Rule 10b-5*, 10 VA. L. & Bus. Rev. 273 (2016)).

declaration alleges a conspiracy between the defendant and Cox to defraud certain banks and trust companies"); *Cheney v. Powell*, 15 S.E. 750, 751 (Ga. 1892) ("the action is in tort, and the declaration alleges conspiracy"). *See also* 1 M. Bigelow, *A Treatise on the Law of Fraud on its Civil Side* § 8 at 246-48 (1888) (section on "Conspirators and the Like"). This Court's decision in *Central Bank*, however, forecloses conspiracy liability in Section 10(b) civil cases for the same reasons it forecloses aiding and abetting. *See, e.g., Dinsmore v. Squadron, Ellenoff, Plesent, Sheinfeld & Sorkin*, 135 F.3d 837, 843-44 (2d Cir. 1998). And unlike aiding and abetting, the SEC (in contrast to the Department of Justice) is given no separate statutory authority to pursue conspiracy claims.

Moreover, even in the conspiracy context, the SEC cites no common law authority for primary liability merely for disseminating the statements of others. *See Zuckerman*, 158 So. at 325-36 (defendant sold land to plaintiff on the basis of promises made by both him and another that the other would buy the land at a profit); *Bank of Commerce*, 160 N.E. at 792 (defendant obtained loans on the basis of bonds he did not own, to build a false "reputation of financial responsibility" aided by another's representations); *Cheney*, 15 S.E. at 750 (representations were made by another based on behind-the-scenes conduct by defendant). Instead, as the Court noted in *Chiarella v. United States*, 445 U.S. 222, 228 n.10 (1980) and the Commission itself noted in *Cady, Roberts & Co.*, 40 S.E.C. 907, 916 n.13, 31 (1961)(*citing Strong v. Repide*, 213 U.S. 419, 430 (1909), and *Pepper v. Litton*, 308 U.S. 295, 307 n.15 (1939)) this Court's common law decisions focused on the presence of a fiduciary duty of disclosure to supply

liability in those instances where the defendant did not himself make a statement. *Stewart v. Wyoming Cattle-Ranche Co.*, 128 U.S. 383, 388 (1888). *See* Sec. Indus. & Fin. Markets Ass'n (SIFMA) & Chamber of Commerce Amici Br. 10-11 & n. 4.

II. The SEC Failed to Show that Petitioner's Own Conduct Falls Within the Text of Sections 10(b) and 17(a)

A. The SEC Fails To Respond To Petitioner's and Amici's Statutory Analysis of Sections 10(b) and 17(a)

The Petitioner's brief also demonstrated that the Petitioner did not violate Section 10(b) because his conduct does not meet the definition of "deception" or "manipulation" that is used in the text of Section 10(b). We also demonstrated that Petitioner did not violate Rule 10b-5 because Rule 10b-5 cannot impose liability beyond the scope of Section 10(b) itself. Petitioner's brief established that Petitioner did not violate either Section 10(b) or Section 17(a)(1) because he did not "use" or "employ" a manipulative, deceptive or fraudulent device or scheme.

Section 10(b) "prohibits only the making of a material misstatement (or omission) or the commission of a manipulative act. . . . We cannot amend the statute to create liability for acts that are not themselves manipulative or deceptive within the meaning of the statute." *Central Bank*, 511 U.S. at 177-78 (1994). *Central Bank* also stated that the "it is inconsistent with settled methodology in § 10(b) cases to extend liability beyond the scope of conduct prohibited by the statutory text." *Id.* at 175, 177. The *Central Bank* Court

further stated it has "refused to allow 10b-5 challenges to conduct not prohibited by the text of the statute." *Id.* at 173.

This Court has concluded that "[t]he language of §10(b) gives no indication that Congress meant to prohibit any conduct not involving manipulation or deception." *Santa Fe Industries v. Green*, 430 U.S. 462, 473 (1977). In *Chiarella* the Court addressed the concept of deception and the Court refused to extend the concept of "deception" beyond the basic common law categories of misrepresentation or a duty to disclose, holding that "[w]hen an allegation of fraud is based upon nondisclosure, there can be no fraud absent a duty to speak . . . premised upon a duty to disclose arising from a relationship of trust and confidence between the parties to a transaction." 445 U.S. 235, 230. The *Chiarella* Court expressly held that the need for either a misrepresentation or a duty to disclose is an essential element of liability under Rules 10b-5(a) or (c). The holdings in *Santa Fe* and *Chiarella* made clear that under Rules 10b-5(a) and (c), just as under Rule 10b-5(b), liability cannot extend beyond three categories: (1) the making of a misrepresentation, (2) an omission or nondisclosure coupled with a duty to speak, and (3) the commission of a manipulative act.

Here, the SEC relies on the absence of any reference to the word "make" in subsections (a) and (c) of Rule 10b-5 and Section 17(a)(1) in arguing against extending *Janus* to those subsections. However, the essential elements of a Section 10(b) claim, namely a misrepresentation, duty to disclose or execution of a manipulative trade, are still required by Section 10(b) itself when pursuing a claim under Rule 10b-5(a) or (c).

Moreover, the SEC's brief focuses almost entirely on the language of Rule 10b-5 and Section 17(a)(1), to the exclusion of Section 10(b). The SEC makes little effort to respond to the arguments of Petitioner or Amici SIFMA & Chamber of Commerce that the scope of Rule 10b-5 is limited by the language of the statute and by the Court's caselaw construing it since *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 212-14 (1976), in which the Court first held that Rule 10b-5 is limited by the text of Section 10(b). Instead, the SEC dismisses four decades of the Court's own precedents as a "gloss" on Section 10(b) entitled to no weight. (Resp. Br. 22) (citing SIFMA & Chamber of Commerce Amic. Br. 9-11) The SEC has thus all but conceded that its argument for Petitioner's primary liability cannot be supported on the basis of either the statutory language of Section 10(b) or the Court's reading of that language in recent decades, and requires the support of the language of Rule 10b-5 to do what Section 10(b) does not. This is exactly the position the Court has rejected since *Ernst*.

The SEC's opposition brief (and that of Amici NASAA) fails to cite a single precedent – whether a case or an administrative proceeding – under any legal rule holding a defendant primarily liable for merely disseminating a statement made by another. While the SEC claims that "the conduct in which petitioner was found to have engaged has long been treated as actionably fraudulent, both under the federal securities laws and under their common-law antecedents" (Resp. Br. 39), it never identifies a single supporting example anywhere in American law.

In other parts of the securities laws when Congress wanted to impose liability for the dissemination of false

statements it did so explicitly. *See* Section 9(a)(5) of the Exchange Act (15 U.S. Code § 78i(a)(5) and Section 17(b) of the Securities Act (15 U.S. Code § 77q(b), which address "circulation," "dissemination," and "publish[ing]" of certain types of statements – language Congress could have, but did not, use in Section 10(b) and 17(a). *See also* SIFMA & Chamber of Commerce Amic. Br. 19-22. Similarly, Section 18(a) of the Exchange Act imposes liability on any defendant who "shall make or cause to be made" a statement that is "false or misleading with respect to any material fact" in "any application, report or document filed" pursuant to the Exchange Act. In Sections 10(b) and 17(a), by contrast, Congress did not prohibit the "causing" of a deceptive device, but instead stopped at the defendant who actually "use[s] or employ[s]" the deceptive device in connection with the purchase or sale of securities (in the case of 10(b)) and the offer or sale of securities (in the case of 17(a)).

The SEC's brief also misstates the legislative history of Section 10(b) when it cites to the Senate Report accompanying the Exchange Act. The SEC conflates the Senate's discussion of Section 9(a)(5) with that of Section 10(b). The SEC claims that "[t]he Senate Report accompanying the Exchange Act identified 'the dissemination of false information' as an example of a 'device[ ]' that is 'subjected to regulation by the Commission,' and it equated the 'devices' prohibited by Section 10(b) with "manipulative or deceptive practices." Resp. Br. 17 (citing S. Rep. No. 792, 73d Cong., 2d Sess. 8-9, 18 (1934)). But this is inaccurate in two ways. The reference on page 8 of the Senate Report plainly describes the conduct specifically banned by Section 9(a)(5), namely the undisclosed

payment of 'touts' to engage in "dissemination of false information and tipster sheets." Senate Report, at 8, 17. As the SIFMA & Chamber of Commerce amici noted, this is the precise point on which the language of Section 9(a)(5) is deliberately and explicitly broader than that of Section 10(b). SIFMA & Chamber of Commerce Amic. Br. 20. Also, the Senate Report describes as "subjected to regulation by the Commission" a different set of price-stabilizing practices (such as "pegging") that are "not abolished by statute" but subject to rulemaking under Section 9(a)(6). Senate Report, at 8-9, 17. None of this discussion in the Senate report refers to Section 10(b), whose legislative history this Court and others have previously found opaque and unenlightening. *See, e.g., Chiarella*, 445 U.S. at 226; *Ernst*, 425 U.S. at 201-03.

Instead of addressing Petitioner's and amici's statutory Section 10(b) arguments, the SEC relies extensively on pre-1976 authorities, on lower-court Section 17 precedents, on the SEC's own interpretations (to which the Court need not defer) and on cases construing statutory language (such as the mail fraud statute) not found in Section 10(b). The SEC's brief also places heavy reliance on the statutory term "scheme" – found in Section 17(a)(1), but not in Section 10(b) – despite the absence of any finding in this matter by the D.C. Circuit, the Commission, or the Administrative Law Judge of a "scheme," which is a fact the SEC ignores.

B. The SEC Cites Inapposite Case Law and Statutes To Support Its Argument Regarding Petitioner's Section 10(b) Liability

The SEC relies on a variety of cases that have nothing to do with the question of whether a person who disseminated a misstatement made by another can be held primarily liable for that misstatement. For example, the SEC cites Section 10(b) cases that explicitly avoided deciding the question of liability for defendants who neither made a statement nor owed a duty to disclose. In *Superintendent of Ins. of N.Y. v. Bankers Life & Cas. Co.*, 404 U.S. 6, 8 n.1, 9-10 (1971), which the SEC presents as a case about "false asset reports," Resp. Br. 16 & 18, this Court held that Section 10(b) was violated when a seller of bonds was deceived about the value it received in the sale; the Court expressly declined to address the liability of individual defendants or other aspects of the transaction. *Id.* at 13 & n. 10. Likewise, *SEC v. National Securities, Inc.*, 393 U.S. 453, 467 (1969), stands for the unremarkable proposition that Section 10(b) governs misrepresentations in proxy statements sent to shareholders to induce approval of a merger; no issues of liability for particular defendants was considered. *Id.* at 465 ("[I]n deciding this particular case, remembering what is not involved is as important as determining what is.").

The SEC reaches even further to rely on dicta in *Chadbourne & Parke LLP v. Troice*, 134 S. Ct. 1058, 1063 (2014). Resp. 30. But *Chadbourne* was construing a different statute, the Securities Litigation Uniform Standards Act, which contains two alternative

provisions: "(A) a misrepresentation or omission of a material fact in connection with the purchase or sale of a covered security; or (B) that the defendant used or employed any manipulative or deceptive device or contrivance in connection with the purchase or sale of a covered security." *Id.* at 1064 (quoting 15 U.S.C. § 78bb(f)(1)(A)-(B)). *Chadbourne* in no way purported to construe Section 10(b).

Finally, the SEC invokes the mail fraud statute (Resp. 17), but this statute says nothing about Section 10(b), and is not helpful to the construction of Section 17(a)(1), either. The mail fraud statute speaks of a "scheme or artifice to defraud," but as noted above, Section 10(b) makes no reference to "schemes," and even regarding the Section 17(a)(1) claim, neither the D.C. Circuit nor the Commission or the Administrative Law Judge found a scheme on the record in this case. What the SEC does not do, in regard to Section 17(a)(1), is explain what the elements of a violation of that statute are or how they differ from the simple making of a misrepresentation, despite Circuit authority -- which the SEC ignores -- suggesting that a fraudulent scheme under Section 17(a)(1) may require "conduct beyond just misrepresentations or omissions." *SEC v. Quan*, 817 F.3d 583, 589 (8th Cir. 2016) (quoting jury instructions). The SEC also fails to demonstrate how Petitioner's conduct falls under Section 17(a)(1)'s prohibitions. In any event, none of the mail fraud cases cited by the SEC prove its point. *Durland v. United States*, 161 U.S. 306, 510-11 (1896), for example, involved letters written directly by the defendant to investors. The SEC also cites to *United States v. Maze*, 414 U.S. 395, 406 (1974), without

disclosing that it is citing Chief Justice Burger's dissent and that the conviction in *Maze* was reversed.

III. The SEC's Argument that the Petitioner Has Taken a Different Factual Position in the Court Below is Without Merit

The SEC for the first time now argues that Petitioner is taking an inconsistent factual position in this Court than what he took below regarding his belief in the accuracy of the statements in the emails he sent. The SEC argues that there is a conflict between Petitioner's argument in the D.C. Circuit that at the time the emails were sent Petitioner believed the statements to be true and the argument in this Court (and the court below) that he didn't draft or carefully read the emails.[4] The SEC argues that "[p]etitioner could not have believed the statements to be true, as he argued to the court of appeals, if he did not read them." (Resp. Br. 19)

However, there is no conflict because in the D.C. Circuit Petitioner argued that his belief in the accuracy of the emails was based on the fact that the emails were prepared by his boss, the owner of Charles Vista, and Petitioner had no reason to doubt the veracity of

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[4] In mischaracterizing Petitioner's arguments the SEC takes statements in Petitioner's brief out of context and wholly ignores the Petitioner's Facts section of the brief, which states Petitioner's "emails were copy and pasted from his boss" and that "Lorenzo testified that he sent the emails without thinking about the contents." (Pet. Opening Br. 10)(citations omitted). Ultimately whether Petitioner read the emails or not before sending them is of no moment because Petitioner has not challenged the D.C. Circuit's finding with regards to scienter.

the statements that were prepared by his boss. Petitioner has never argued, either in this Court or in the D.C. Circuit, that his belief in the accuracy of the statements in the emails was based on his having read the emails and performed an independent analysis of the content of the emails to determine their truth or falsity. In fact, in his brief in the D.C. Circuit Petitioner specifically argued that "Petitioner had a good faith belief in the accuracy of the statements contained in the email because the statements came from...the owner of Charles Vista" (Pet. D.C. Circuit Opening Br. 22). Petitioner recognizes that the D.C. Circuit rejected this argument but there is no inconsistency between the position the Petitioner took in the D.C. Circuit and the position he takes in this Court. Contrary to the SEC's statement that Petitioner is attempting to relitigate scienter (Resp. Br. 19), Petitioner has not challenged the D.C. Circuit's finding of scienter in this appeal and scienter is not part of the question presented to this Court.

The SEC's argument that Petitioner took a different position in the D.C. Circuit than he takes in this Court is also based on the SEC conflating two separate arguments Petitioner made in the D.C. Circuit. These two arguments are the argument in the D.C. Circuit that the statements were not objectively false and the argument that Petitioner did not act with scienter. Petitioner argued in the D.C. Circuit that the statements in the emails were objectively true and, as a result, the SEC did not prove one of the elements its Rule 10b-5 claim. (Pet. D.C. Circuit Opening Br. 12-18) Petitioner based this argument on documentary evidence found in SEC filings and exhibits introduced at the administrative hearing and not on any

independent investigation that Petitioner undertook. *Id.* None of these arguments have anything to do with Petitioner's scienter and, more importantly, none of these arguments have been advanced by the Petitioner in this Court and they are simply not part of the issues the Court has to address.

Finally, the SEC's meritless arguments that Petitioner is taking a different view of the facts in this Court are waived because the SEC did not raise them in its brief in opposition to the cert petition. Supreme Court Rule 15.2. Rule 15.2 provides in pertinent part:

> In addition to presenting other arguments for denying the petition, the brief in opposition should address any perceived misstatement of fact or law in the petition that bears on what issues properly would be before the Court if certiorari were granted. Counsel are admonished that they have an obligation to the Court to point out in the brief in opposition, and not later, any perceived misstatement made in the petition. Any objection to consideration of a question presented based on what occurred in the proceedings below, if the objection does not go to jurisdiction, may be deemed waived unless called to the Court's attention in the brief in opposition.

This Court's precedent demonstrates that the Court refuses to address issues a respondent raised for the first time in merits briefing and not in a respondent's brief in opposition to the Petition for Writ of Certiorari. The Court also has also, on occasion, treated as being established statements of fact from the petition that the respondent didn't contest in its brief in opposition.

See, e.g. Corcieri v. Salazar, 555 U.S. 379, 395-396 (2009).

> Respondents' brief in opposition declined to contest [the assertion that the Narragansett Indian Tribe ... was neither federally recognized nor under the jurisdiction of the federal government]. Under our rules, that alone is reason to accept this as fact for purposes of our decision in this case. *See* this Court's Rule 15.2. We therefore reverse the judgment of the Court of Appeals. (citations omitted)

The SEC's Brief in Opposition to the Petition for Writ of Certiorari never suggested Petitioner's factual position in the petition was inconsistent with his position before the D.C. Circuit and it is simply too late for the SEC to raise arguments based on record materials it never cited in its brief in opposition.

IV. Affirming the D.C. Circuit Would Erase the Distinction Between Primary and Secondary Liability

The SEC argues that the D.C. Circuit's decision preserves the distinction between primary and secondary liability because Petitioner's own conduct makes him a primary violator of the securities laws. But the only conduct Petitioner was found to have engaged in was his producing and sending the emails in question. (Resp. Br. 33) It was this ministerial conduct alone that the D.C. Circuit relied on when holding that Petitioner's dissemination of the emails constituted employing a deceptive 'device,' 'act,' or 'artifice to defraud' even though he was not the maker of the statements in the emails.

The D.C. Circuit's low threshold for primary liability gives virtually no weight to Congress's well thought out distinction between primary and secondary liability as reflected in the language of the main aiding and abetting statutes, Section 15(b) of the Securities Act, 15 U.S.C. § 77o(b), and Section 20(e) of the Exchange Act, 15 U.S.C. § 78t(e). As amici Law Professors argued:

> Congress said a key element of aiding and abetting is that the defendant must provide substantial assistance. Under the current version of Section 20(e), the SEC may bring an action against "any person that knowingly or recklessly provides substantial assistance to another person" that violated the Exchange Act or its regulations. If substantial assistance is required for aiding and abetting, primary liability must require more. If substantial assistance were enough for primary liability, no difference between a primary actor and an aider and abettor would exist. *Central Bank* and Congress's adoption of aiding and abetting provisions would have served no purpose. The statutory substantial assistance requirement tells us that a difference between primary liability and aiding and abetting must exist, and it must be meaningful and substantial. (Law Professors Amici Br. 8)

Not only does a low threshold for primary liability undermine Congress's determination that "substantial assistance" is required for aiding and abetting liability it also conflicts with this Court's decisions in *Central Bank of Denver, NA v. First Interstate Bank of Denver,*

NA, 511 U.S. 164 (1994), *Janus*, and *Stoneridge*. Those decisions show that primary liability under Rule 10b-5 must be closely linked to a misstatement or misconduct that deceived a securities offeree, buyer, or seller.

V. Affirming the D.C. Circuit Would Result in Numerous Meritless Lawsuits

The difference between primary and secondary liability is of critical importance in private securities litigation because under *Central Bank* plaintiffs in private securities litigation, including class actions, may not assert claims for aiding and abetting liability. Petitioner's brief demonstrated that affirming the D.C. Circuit's decision would undermine *Central Bank* by raising significant uncertainty about the scope of primary liability. *Central Bank* held that liability under Section 10(b) is " 'an area that demands certainty and predictability.' " 511 U.S. at 188 (*quoting Pinter v. Dahl*, 486 U.S. 622, 652 (1988)). This is because uncertainty drives up the costs of numerous legitimate transactions and eliminates some altogether. *See* 511 U.S. at 188-89. Affirming the D.C. Circuit's decision would in substance revive the implied cause of action against aiders and abettors, a result soundly rejected by the *Stoneridge* Court.

The SEC's response is that the Private Securities Litigation Reform Act of 1995 (the "PSLRA") (Pub. L. No. 104-67, 109 Stat. 737), with its heightened pleading standards and other requirements for private lawsuits and the Securities Litigation Uniform Standards Act of 1998, 112 Stat. 3227, which curtailed plaintiffs' ability to evade the PSLRA's limitations on federal securities-fraud litigation by bringing class-action suits under state rather than federal law, would protect defendants

from meritless private lawsuits. (Resp. Br. 38-39) However, the SEC's argument misses the mark. "[P]laintiffs with weak claims [can] extort settlements" from "innocent" companies that nevertheless fear "extensive discovery and the potential for uncertainty and disruption in a lawsuit." *Stoneridge*, 552 U.S. at 163; *see also Merrill Lynch, Pierce, Fenner & Smith Inc. v. Dabit*, 547 U.S. 71, 80–81 (2006). (SIFMA & Chamber of Commerce Amici Br. 24) The SIFMA & Chamber of Commerce Amici Brief further discusses how private lawsuits can be employed "abusively to impose substantial costs on companies and individuals whose conduct conforms to the law." (SIFMA & Chamber of Commerce Amici Br. 24) The SEC's reliance on the PSLRA to protect defendants from meritless lawsuits is particularly misguided because "[s]ince Congress enacted the PSLRA in 1995, securities class actions have wiped out over $701 billion in investment value and given shareholders only $90 billion. (SIFMA & Chamber of Commerce Amici Br. 25).

The SEC's PSLRA argument, moreover, would put an unsupportable interpretation on Congress' specific response to *Central Bank* in PSLRA §104. *Stoneridge*, 552 U.S. at 162. In response to *Central Bank*'s elimination of aiding and abetting liability in 1995 Congress passed Section 20(e) of the Exchange Act as part of the PSLRA. Section 20(e) restored the SEC's ability to bring actions for aiding and abetting against anyone who "knowingly or recklessly provides substantial assistance to another person" in a violation of the federal securities laws. Section 20(e) did not restore the ability of private plaintiffs to bring aiding and abetting claims. The D.C. Circuit's revival of the

implied cause of action against aiders and abettors undermines Congress's determination that this class of defendants should be pursued only by the SEC. *Id.*

CONCLUSION

For the foregoing reasons the judgment of the D.C. Circuit holding that Petitioner violated Section 10(b) of the Exchange Act, Rules 10b-5(a) and (c) and Section 17(a)(1) of the Securities Act should be reversed.

Respectfully submitted,

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IN THE

Supreme Court of the United States

FRANCIS V. LORENZO,
Petitioner,

v.

SECURITIES AND EXCHANGE COMMISSION,
Respondent.

On a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF OF THE NORTH AMERICAN SECURITIES ADMINISTRATORS ASSOCIATION, INC., AS *AMICUS CURIAE* IN SUPPORT OF RESPONDENT

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STATEMENT OF INTEREST[1]

The North American Securities Administrators Association, Inc. ("NASAA") is the non-profit association of state, provincial, and territorial securities regulators in the United States, Canada and Mexico. NASAA has 67 members, including the securities regulators in all 50 states, the District of Columbia, Puerto Rico, and the U.S. Virgin Islands. Formed in 1919, NASAA is the oldest international organization devoted to protecting investors from fraud and abuse in the offer and sale of securities.

NASAA's U.S. members are responsible for regulating transactions under state securities laws, commonly known as "Blue Sky Laws." *See generally* LOUIS LOSS ET AL., SECURITIES REGULATION 55-251 (6th ed. 2014). Our U.S. members' principal activities include: registering local securities offerings, licensing and examining brokers and investment advisers who sell securities or provide investment advice, and initiating enforcement actions to combat fraud and other violations of state securities laws. One of NASAA's goals is to foster greater uniformity across state and federal securities laws, though the overriding mission of NASAA and its members is to

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[1] Pursuant to U.S. Sup. Ct. Rule 37.6, counsel for *amicus* affirms that no party other than *amicus* and its counsel authored this brief, in whole or in any part, and that no person or entity other than *amicus* or *amicus's* counsel has made a monetary contribution to the preparation and submission of this brief. The parties have provided their written consent for the filing of this *amicus* brief.

protect investors, particularly retail investors, from fraud and abuse.

NASAA supports the work of its members and the investing public by, among other things, promulgating model rules, providing training opportunities, coordinating multi-state enforcement actions and examinations, and commenting on proposed legislation and rulemakings. NASAA also offers its legal analysis and policy perspective to state and federal courts as *amicus curiae* in important cases involving the interpretation of state and federal securities laws, securities regulation, and investor protection. This is one of those cases. NASAA and its members have an interest in this matter because this case has important implications for public and private antifraud actions brought under federal securities law and, potentially, under state securities laws as well.

NASAA is submitting this *amicus curiae* brief to provide its views on this litigation and to rebut arguments made by Petitioner and his two *amici* in briefs filed August 27, 2018, the *Brief of Amici Curiae Securities Law Professors in Support of Petitioner* (hereinafter, the "Professors' Brief") and the *Brief of Amici Curiae Securities Industry and Financial Markets Association and Chamber of Commerce of the United States of America Supporting Petitioner* (hereinafter, the "SIFMA/Chamber Brief").

SUMMARY OF ARGUMENT

Petitioner was found liable for making material misstatements and engaging in a fraudulent scheme in violation of Section 10(b) of the Securities Exchange Act of 1934 and SEC Rule 10b-5 thereunder by the U.S. Securities and Exchange Commission (the "SEC" or "Commission"). *See In re Francis V. Lorenzo*, SEC Release No. 34-74836 (Apr. 29, 2015). A majority of the judges on a three-judge panel of the Court of Appeals for the District of Columbia Circuit (the "Circuit Court") found substantial evidence to support nearly all of the Commission's findings. *See Lorenzo v. SEC*, 872 F.3d 578 (D.C. Cir. 2017). Arguing that the facts and law do not support the Circuit Court's decision, Petitioner seeks to overturn it. Petitioner is wrong.

The Circuit Court properly found Petitioner liable for engaging in a fraudulent scheme within the meaning of Section 10(b) and Rules 10b-5(a) and (c). Petitioner's act of knowingly sending two materially false and misleading emails to effectuate the sale of securities his brokerage firm was underwriting is precisely the sort of fraudulent scheme that Congress intended the securities laws to prevent and punish.

In addition, although not squarely before the Court, the Commission properly found in its underlying administrative court decision that Petitioner was also liable under Rule 10b-5(b) as the "maker" of the misstatements in his two emails pursuant to *Janus Capital Grp. v. First Derivative Traders*, 564 U.S. 135 (2011). Finally, given the findings of liability under Rule 10b-5, Petitioner's

liability under Section 17(a) of the Securities Act of 1933 logically follows as well.

In contrast, Petitioner and his *amici* ask this Court to significantly limit the scope of liability under Rules 10b-5(a) and (c). They assert this is necessary to maintain fidelity with the Court's relevant precedents, to achieve consistency between Section 10(b) and Section 17(a), and because the nation's securities markets would be imperiled otherwise. None of these points are valid. The Circuit Court's opinion affirming defendant's culpability under Rules 10b-5(a) and (c) was correct and on all fours with this Court's jurisprudence. This is aptly demonstrated by both the Circuit Court's opinion and other relevant precedent cited below. Furthermore, Petitioner's purported concern that the securities markets are or will be harmed by enforcing the securities laws is baseless. To the contrary; the securities laws, and Rules 10b-5(a) and (c) in particular, were intended first and foremost to protect investors and the securities markets generally from fraud.

ARGUMENT

I. THE CIRCUIT COURT CORRECTLY HELD THERE WAS SUBSTANTIAL EVIDENCE TO SUPPORT THE SEC'S FINDING THAT PETITIONER ENGAGED IN AN UNLAWFUL SECURITIES SCHEME.

Section 10(b) makes it unlawful "to use or employ . . . any manipulative or deceptive device or contrivance" in connection with the purchase or sale

of a security. 15 U.S.C. § 78j(b). SEC Rule 10b-5 promulgated thereunder contains three subparagraphs that diagram broad categories of such manipulative or deceptive devices: (a) fraudulent schemes or artifices, (b) fraudulent misrepresentations or omissions, and (c) fraudulent practices or courses of business. 17 C.F.R. § 240.10b-5. The Court has long held that Section 10(b) and Rule 10b-5 "should be construed not technically and restrictively, but flexibly to effectuate [their] remedial purposes" of protecting investors and establishing fair and orderly markets. *SEC v. Zandford*, 535 U.S. 813, 819 (2002) (internal quotations and citations omitted).

Rule 10b-5 claims typically fall into two general categories: misrepresentation claims, which proceed under Rule 10b-5(b), and "scheme liability" claims, which proceed under Rule 10b-5(a) or (c). *E.g.*, *In re DVI, Inc. Sec. Litig.*, 639 F.3d 623, 643 n.29 (3d Cir. 2011) ("We refer to claims under Rule 10b–5(a) and (c) as 'scheme liability claims' because they make deceptive conduct actionable, as opposed to Rule 10b–5(b), which relates to deceptive statements."), *abrogated on other grounds by Amgen Inc. v. Conn. Ret. Plans & Trust Funds*, 568 U.S. 455 (2013). The term "scheme liability" is a relatively recent jurisprudential coinage; the first reported opinion to use this term was in 2005. *See In re Global Crossing Ltd. Sec. Litig.*, No. 02 Civ. 910(GEL), 2005 WL 1907005, *2 n.5 (S.D.N.Y. Aug. 8, 2005). This is not because the concept of "scheme liability" did not previously exist; Rules 10b-5(a) and (c) have prohibited fraudulent securities schemes since the

rule was enacted in 1942. *See* Exchange Act Release No. 3230 (May 21, 1942). The relevant jurisprudential question is, thus, to what extent causes of action pled under Rule 10b-5(a) or (c), such as the case at bar, are valid.

NASAA member state securities regulators combat securities fraud on a daily basis. These securities frauds encompass a dizzying array of bad behavior – including offering frauds, market manipulation schemes, insider trading, Ponzi schemes, theft or conversion, and breach of a fiduciary or other duty by a securities professional –and often involve a mélange of fraudulent misrepresentations and schemes to defraud. For example, a Ponzi schemer typically perpetuates his scam through misrepresentations (*e.g.*, false investor reports) and deceptive schemes (*e.g.*, repaying earlier investors with deposits from later investors). Most securities frauds thus cannot be categorized as solely a misrepresentation or a scheme liability case, but instead include both false representations and schemes to defraud. The instant litigation is just such a case. Petitioner engaged in both a deceptive scheme to defraud and made misleading statements. Since Petitioner violated two separate sections of the securities laws, he should be held accountable under both sections. The text of Rule 10b-5 makes it clear that the subsections of the Rule are complementary and should not be interpreted in a way that works against Congress's purpose in enacting Section 10(b), which was to prohibit securities fraud in any of its myriad forms. *Chiarella v. United States*, 445 U.S.

222, 234-35 (1980) ("Section 10(b) is aptly described as a catchall provision, but what it catches must be fraud.").

Petitioner and his *amici* ask this Court to hold that primary liability under Rule 10b-5(a) or (c) can never be predicated solely on a misrepresentation or omission. They argue that frauds predicated on misstatements should always proceed under Rule 10b-5(b) only, and that this Court should create out of thin air an addendum to Rule 10b-5(a) and (c) that limits scheme liability to those schemes that do not rely on misrepresentations. This is necessary and appropriate, they claim, so as not to render meaningless the boundaries on primary liability under Rule 10b-5(b) this Court set forth in *Central Bank of Denver v. First Interstate Bank of Denver*, 511 U.S. 164 (1994) and *Janus Capital Group v. First Derivative Traders*, 564 U.S. 135 (2011). *See* Petitioner's Brief at 17-18; Professors' Brief at 10-11; SIFMA/Chamber Brief at 15-17. Petitioner and his *amici* are mistaken. It is plain from the language of Rule 10b-5 that Primary liability can exist under Rule 10b-5(a) or (c)—indeed, such liability has always existed—for fraudulent schemes predicated upon material misrepresentations or omissions. What is more, this conclusion does no damage to this Court's decisions in *Central Bank*, *Janus* or otherwise.

A. Insider Trading Is Scheme Liability Predicated Upon Misrepresentations or Omissions.

That liability can exist under Rule 10b-5(a) or (c) based purely on a material misrepresentation or omission is illustrated by this Court's precedent regarding insider trading. No statute or SEC rule expressly prohibits insider trading. Rather, insider trading is unlawful under Section 10(b) and Rule 10b-5 because of the inherent unfairness when one party takes advantage of material nonpublic information in violation of a duty of confidentiality owed to another party. *Dirks v. SEC*, 463 U.S. 646, 654 (1983). Under either the so-called classical or misappropriation theories, insider trading "satisfies § 10(b)'s requirement that chargeable conduct involve a 'deceptive device or contrivance' used 'in connection with' the purchase or sale of securities." *United States v. O'Hagan*, 521 U.S. 642, 653 (1997). The deceptive device in insider trading is "feigning fidelity to the source of information." *Id.* at 655. *See also Dirks*, 463 U.S. at 660 (explaining that tippees assume the disclosure duties of their tippers).

Insider trading liability is tied to Rule 10b-5(a) and (c), not Rule 10b-5(b), notwithstanding that insider trading is at root a misrepresentation crime. *See O'Hagan*, 521 U.S. at 651 (citing Rule 10b-5(a) and (c) as the sources of legal liability); *Chiarella*, 445 U.S. at 225-26 (1980) (same). This is consistent with the text of Rules 10b-5(a) and (c), which are written more broadly than paragraph (b). As this Court

explained long ago in *Affiliated Ute Citizens of Utah v. United States*, 406 U.S. 128 (1972), "the second subparagraph of [Rule 10b-5] specifies the making of an untrue statement of a material fact and the omission to state a material fact. *The first and third subparagraphs are not so restricted.*" *Id.* at 152-53 (emphasis added).

Even in cases in which a defendant affirmatively lies about his intention not to trade or otherwise makes a misstatement that would clearly give rise to a potential Rule 10b-5(b) cause of action, liability for insider trading is still treated as a fraudulent *scheme* for which liability resides in Rule 10b-5(a) or (c). *See, e.g., SEC v. Rocklage*, 470 F.3d 1 (1st Cir. 2006) (affirming denial of the defendant's motion to dismiss insider trading charges under Rule 10b-5(a) and (c) where the tippee had misrepresented her intention not to tip or trade on the material nonpublic information); *SEC v. Yun*, 327 F.3d 1263 (11th Cir. 2003) (same). A defendant's nondisclosure of the intention to trade, or his affirmative misstatements with respect thereto, is thus an equally deceptive "device, scheme or artifice" under Rule 10b-5(a) or "act, practice, or course of business" under Rule 10b-5(c).

Insider trading is not the only type of scheme liability predicated upon material misrepresentations or omissions that courts have recognized. Other such schemes include a broker-dealer or investment adviser's selective misallocation of securities trades, colloquially and colorfully known as "cherry-picking" (*e.g., SEC v. K.W. Brown & Co.*, 555 F. Supp. 2d 1275

(S.D. Fla. 2007), falsification of corporate financial records (*e.g.*, *SEC v. Monterosso*, 756 F.3d 1326 (11th Cir. 2014), and arrangement of sham transactions to give a false appearance of business operations (*e.g.*, *In re Parmalat Sec. Litig.*, 376 F. Supp. 2d 472 (S.D.N.Y. 2005). "Accordingly, scheme liability does not preclude, outright, claims based upon a scheme to misrepresent or omit material facts." *SEC v. Goldstone*, 952 F. Supp. 2d 1060, 1206 (D.N.M. 2013).

B. Liability under Rule 10b-5(a) or (c) is Predicated on Whether the Defendant's Conduct was Deceptive or Manipulative

The plain text of Rules 10b-5(a) or (c) makes clear that a fraudulent scheme claim is predicated not on whether a material misrepresentation or omission occurred, but rather on whether the defendant's conduct was deceptive or manipulative. Indeed, one district court has called it "nonsensical" that scheme liability cannot exist where the purpose of the scheme was to make a misstatement. *SEC v. Lucent Tech.*, 610 F. Supp. 2d 342, 359 (D.N.J. 2009). The existence of a deceptive or manipulative act has always been the *sine qua non* of liability under Rule 10b-5, and this notion is rooted in the actual text of Section 10(b): "It shall be unlawful for any person, directly or indirectly, . . . to use or employ, in connection with the purchase or sale of any security . . ., *any manipulative or deceptive device or contrivance* . . . ." 15 U.S.C. § 78j(b) (emphasis added).

Conduct is *manipulative* within the meaning of Section 10(b) and Rule 10b-5 when it improperly

affects the market for a security. The word manipulative "is virtually a term of art" and "connotes intentional or willful conduct designed to deceive or defraud investors by controlling or artificially affecting the price of securities." *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 199 (1976). Activities such as price rigging, wash sales, matched orders, layering, or spoofing are manipulative because they artificially affect the normal functioning of the securities markets. *See Santa Fe Indus., Inc. v. Green*, 430 U.S. 462, 476 (1977); *SEC v. Lek Sec. Corp.*, 276 F. Supp. 3d 49, 54-56 (S.D.N.Y. 2017).

While the Court has not yet defined *deceptive* conduct for purposes of Section 10(b) and Rule 10b-5 (*Regents of the Univ. of Calif. v. Credit Suisse First Boston (USA), Inc.*, 482 F.3d 372, 389 (5th Cir. 2007)), it has held that conduct itself can be deceptive – *i.e.*, deception does not require that a misrepresentation or omission has occurred – and that misrepresentations or omissions can themselves constitute deceptive acts. *Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc.*, 552 U.S. 148 (2008).

Lower courts presented with this question generally pose the following test for deception: Did the defendant's conduct give anyone a false impression of material fact about a security (or could anyone have reasonably gotten such a false impression)? *See, e.g.*, *SEC v. Dorozhko*, 574 F.3d 42, 50 (2d Cir. 2009) ("'deceptive' covers a wide spectrum of conduct involving cheating or trading in falsehoods); *United States v. Finnerty*, 533 F.3d 143, 148 (2d. Cir. 2008)

(deception "entails some act that gives the victim a false impression"); *Clark v. Capital Credit & Collection Servs.*, 460 F.3d 1162, 1174 n.10 (9th Cir. 2006) ("Something is deceptive if it tends or has the power to 'give a false impression.'"). Deception thus can be satisfied either in actuality (*i.e.*, one or more victims really were deceived) or potentially (*i.e.*, a reasonable person in the victim's position could have been deceived). Applying this same test to determine whether a defendant's conduct was deceptive or manipulative pursuant to Rules 10b-5(a) and (c) as the Circuit Court did here, is not at all unfair or unreasonable, nor does such a test ensure that the SEC or a private plaintiff will prevail. For example, courts in the Second Circuit have taken this approach in government prosecutions and the government has still lost. *See Finnerty*, 533 F.3d at 148-49.

C. Petitioner's Conduct was Deceptive.

As the Circuit Court held, the facts at issue here are sufficient to demonstrate that Petitioner committed a deceptive act and is liable under Rules 10b-5(a) and (c). The Circuit Court found substantial evidence in support of the Commission's conclusions that Petitioner violated Rule 10b-5(a) and (c) when, at the request of his boss, Petitioner sent two emails to potential investors in a debenture offering and included in his emails the following material falsehoods, the untruth of which *was known* to Petitioner: (i) the issuer had over $10 million in confirmed assets; (ii) the issuer had purchase orders and letters of intent for over $43 million in orders; and

(iii) Petitioner's firm had agreed to raise additional monies to repay any purchasers in the future if necessary. *See* 872 F.3d at 581. The Circuit Court agreed with the Commission that Petitioner took an "active role in producing and sending the emails [which] constituted employing a deceptive device, act, or artifice to defraud." *Id.* at 589 (internal citation and quotations omitted).

With respect to the Petitioner's deception, his role as director of investment banking at his brokerage firm was known to the potential investors (or at least fully disclosed to them), and Petitioner also personally vouched for the veracity of the information in his two emails. *Id.* at 590. He was not a ministerial employee, and investors reasonably expected that he had access to sensitive or even privileged information about the offering. The Circuit Court rightly concluded that Petitioner's conduct reasonably caused the investors receiving the emails to have a false impression of material facts about the debenture offering. *Id.* at 583-86.

The Circuit Court also found no incongruity between this result and its separate conclusion that Petitioner was not liable for making the misstatements within the meaning of Rule 10b-5(b), as the Court interpreted that term in *Janus*. The Circuit Court reasoned that, depending on the facts and circumstances of each case, someone in Lorenzo's shoes could be potentially liable on a scheme liability theory, on a misstatement theory, on both theories or on neither theory: "One can readily imagine persons whose ministerial acts in connection with false

statements would fail to qualify either as 'making' the statements or as 'employing' any fraudulent device. Lorenzo, in our view, is not such a person." *Id* at 595. The Circuit Court's scheme liability analysis was entirely correct.[2]

Investors reasonably expect, and the plain text of Rule 10b-5 permits, a potential cause of action against a broker-dealer that sells them a security pursuant to information it knew was materially false (or where the broker-dealer was willfully blind or otherwise reckless with respect thereto). A contrary result, such as advocated for by Petitioner and in the SIFMA/Chamber Brief, would give broker-dealers and other securities professionals a free pass to knowingly sell securities pursuant to materially false and misleading information so long as the broker was not the original creator of the misstatements. This is precisely the sort of *caveat emptor* approach that Congress intended the securities laws to prevent. *See Kokesh v. SEC*, — U.S. —, 137 S. Ct. 1635, 1640 n.1 (2017).

D. The Circuit Court's Opinion Is Consistent with *Central Bank* and *Janus*.

The gravamen of Petitioner and his *amici's* complaints with the Circuit Court's opinion is that it would supposedly render *Central Bank* and *Janus* "meaningless." *See* Petitioner's Brief at 21; Professor's Brief at 3; SIFMA/Chamber Brief at 5.

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[2] As discussed in Part II below, Petitioner was also a "maker" under *Janus*.

But *Central Bank* and *Janus* are not so feeble. The Circuit Court's opinion, together with other decisions such as *SEC v. Big Apple Consulting USA, Inc.*, 783 F.3d 786 (11th Cir. 2015), more than adequately explain why holding Petitioner liable on a scheme liability theory is completely consistent with *Central Bank*, *Janus* and the Court's other precedents.

Central Bank stands for the proposition that private litigants cannot bring aiding and abetting claims under Section 10(b) and Rule 10b-5. *See id.*, 511 U.S. at 191. After *Central Bank*, private rights of action are valid against primary violators only. But what is the dividing line between primary and secondary liability? *Janus* established this boundary for Rule 10b-5(b) claims: a defendant is primarily liable for making a material misrepresentation or omission in violation of Rule 10b-5(b) if the person had "ultimate authority" over it. *Janus*, 564 U.S. at 142. The Court has not established a similar bright line for primary versus secondary liability under Rule 10b-5(a) or (c), though. Instead, Courts currently evaluate this question on a case-by-case basis based on the plain text of the rule and Section 10(b).

Rule 10b-5(a) makes it unlawful "to *employ* any device, scheme, or artifice to defraud." 17 C.F.R. § 240.10b-5(a) (emphasis added). Rule 10b-5(c) makes it unlawful "to *engage* in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person." 17 C.F.R. § 240.10b-5(c) (emphasis added). Like the operative word "make" in Rule 10b-5(b), the operative words in

paragraphs (a) and (c) – "employ" and "engage in" – are not difficult to define. The dictionary defines "employ" in this context as "to put to use or service" and "engage in" as "to involve oneself or become occupied / participate." THE AMERICAN HERITAGE COLLEGE DICTIONARY at 460, 464 (4th ed. 2004).

The Court's diagramming of the word "make" in *Janus* indicates that "employ" or "engage in" are broader terms.[3] This result should not be surprising; *Affiliated Ute* said as much forty years ago. *See id.*, 406 U.S. at 152-53. *Janus* reasoned that "make" is akin to "proclaim" or "state." *Id.*, 564 U.S. at 142. The act of proclaiming or stating something is linear; regardless of how a statement is created, responsibility ultimately rests with some authority.[4] Given this, *Janus* concluded, "the maker of a statement is the person or entity with ultimate authority" over it. *Id.* In contrast, the terms "employ" or "engage in" are not so delimited. Multiple persons of independent agency and identity can readily be said to "employ" or "engage in" some conduct, statement or activity. *Janus's* ultimate authority standard thus does not transfer to assessing primary liability under Rule 10b-5(a) or (c).

The Professors' Brief posits that the dividing line between primary and secondary scheme liability should be inferred from the general law of aiding and

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[3] The term "any" – utilized in both 10b-5(a) and (c), is, of course, as broad as the English language permits.

[4] As discussed in Section II, *supra*, this authority could be shared among more than one person.

abetting. They reason that because aiding and abetting requires "substantial assistance" to the underlying violation, "primary liability must require more." Professors' Brief at 8. This approach does not work as a universal rule in the real world of securities frauds. For example, it is a poor rubric for tipper-tippee insider trading cases. Courts routinely hold tippers and tippees equally liable for insider trading even if one of the party's relative culpability vastly exceeded the other's. *E.g.*, *SEC v. Sabrdaran*, 252 F. Supp. 3d 866, 897 (N.D. Cal. 2017) (noting that downstream tippees remote from the underlying breach of fiduciary duty can be held equally liable). *See also Salman v. United States*, — U.S. —, 137 S. Ct. 420 (2016) (rejecting the notion that a tipper must receive a pecuniary or similarly valuable benefit from a tip).

The reasoning in the Professors' posited approach also breaks down upon further testing. For instance, imagine a master/servant situation in which a controlling party has ultimately responsibility for a securities fraud, but the controlled party does all the dirty work. Are they both primary violators? If not, then which one of them is – the controlling party (by virtue of his authority) or the controlled party (because he took all the material steps to perpetrate the fraud)? Convincing arguments could be made in any direction. Similarly, imagine three defendants who conspire to commit a securities fraud and contribute approximately, but not precisely, equally to the scheme (*e.g.*, the first conducts approximately 50% of the misconduct, the second 30%, and the third

20%). Are all three primary violators? Two of them? Just one? To say that a primary violator must do more than merely "substantially assist" in a securities fraud, in the end, teaches us nothing. Instead of the Professors' flawed calculus, a better approach for assessing primary versus secondary scheme liability would be to follow the plain text of the statute and rule, and determine whether each defendant committed a material manipulative or deceptive act. As discussed above, this is precisely what federal courts have been doing for years – and was the approach taken by the Circuit Court below.

II. THE COMMISSION WAS CORRECT THAT PETITIONER WAS A "MAKER" UNDER *JANUS*.

The Circuit Court concluded Lorenzo was not liable under Rule 10b-5(b) because it found that, under the Court's ruling in *Janus*, Lorenzo was not the "maker" of the emails he sent. Although not squarely before the Court, below we explain why the Circuit Court was wrong, providing another avenue for the Court to sustain the Commission's decision.

Under Rule 10b-5(b), it is unlawful to "make any untrue statement of a material fact . . . in connection with the purchase or sale of any security." 17 C.F.R. § 240.10b-5(b). In *Janus*, the Court explained that to "[m]ake" means "to state," not to "create." 564 U.S. at 142-44, 131 S. Ct. 2296. Thus, "[o]ne 'makes' a statement by stating it." *Id.* at 142, 131 S. Ct. 2296. "For purposes of Rule 10b-5, the

maker of a statement is the person or entity with ultimate authority over the statement, including its content and whether and how to communicate it." *Id.* The Court explained:

> Without control, a person or entity can merely suggest what to say, not "make" a statement in its own right. One who prepares or publishes a statement on behalf of another is not its maker. And in the ordinary case, attribution within a statement or implicit from surrounding circumstances is strong evidence that a statement was made by—and only by—the party to whom it is attributed. This rule might best be exemplified by the relationship between a speechwriter and a speaker. Even when a speechwriter drafts a speech, the content is entirely within the control of the person who delivers it. And it is the speaker who takes credit—or blame—for what is ultimately said.

Id. at 142-43, 131 S. Ct. 2296.

After this Court's decision in *Janus*, corporate officers who signed documents containing untrue statements attempted to avoid Section 10(b) liability by arguing that their company or board of directors, rather than the officers themselves, had "ultimate authority" over the statements, and thus that the officers did not "make" the statements. *See, e.g., In re Smith Barney Transfer Agent Litig.*, 884 F. Supp. 2d 152, 163-64 (S.D.N.Y 2012). But this evasive strategy

was roundly rejected by courts. *See id.* (citing cases); *cf. Glickenhaus & Co. v. Household Intern., Inc.*, 787 F.3d 408, 426-27 (7th Cir. 2015) (granting new trial on whether corporate officer "made" false statements in a press release where, among other things, there was no evidence officer signed press release and his name did not appear in the press release) (citing *Peterson v. Winston & Strawn LLP*, 729 F.3d 750, 752 (7th Cir. 2013) (defendant law firm probably not liable for contents of a circular it helped prepare because it "did not sign the document or warrant the truth of its contents")); *Howard v. Everex Sys., Inc.*, 228 F.3d 1057, 1061 (9th Cir. 2000) (a corporate official who "signs a SEC filing containing misrepresentations" is "mak[ing] a statement so as to be liable as a primary violator under § 10(b)").

Even those courts post-*Janus* that have adopted the narrowest definition of a "maker" nevertheless maintain that "officers whose signatures appear on misleading statements may be liable as the 'makers' of those statements." *Livingston v Cablevision Sys. Corp.*, 966 F. Supp. 2d 208, 221 (E.D.N.Y. 2013) (finding *Janus* abrogated the group-pleading doctrine); *see also In re Banco Bradesco S.A. Sec. Litig.*, 277 F. Supp. 3d 600, 640-41 (S.D.N.Y. 2017) (finding the group-pleading/group-published doctrine no longer viable after *Janus*, and limiting the "maker" of a statement to those who, for example, "signed the company's statement; ratified and approved the company's statement; or where the statement is attributed to the executive" (quoting *In re Fannie Mae 2008 Sec. Litig.*, 891 F. Supp. 2d 458,

473 (S.D.N.Y. 2012))). Thus, "*Janus* did not change the longstanding rule that corporate officials are liable for misstatements to which they give their imprimatur." *In re Smith Barney*, 884 F. Supp. 2d at 164. Indeed, prior to the ruling of the court below, it appears that courts unanimously have held that a corporate officer's signature or similar imprimatur on a corporate statement renders him a "maker" of the statement.

Here, substantial evidence supports the Commission's finding that Lorenzo had ultimate authority over the untrue statements in his emails, and was thus a "maker" of them for purposes of Rule 10b-5(b). Lorenzo, who was the director of investment banking at a registered broker-dealer, (1) signed off each email with "Truly, Francis V. Lorenzo," his title "Vice President—Investment Banking," and his direct phone number; (2) sent the emails from his own account; (3) invited recipients to "Please call with any questions"; and (4) testified that he understood that, by sending the emails, he was "putting his own reputation on the line."

This evidence is more than sufficient to show that Lorenzo possessed ultimately authority over the emails. First—and dispositive on its own—Lorenzo signed the emails. Just like a corporate officer who puts her signature on a corporate statement written by others, thus adopting the statement as her own, Lorenzo adopted the emails as his own by signing them with his name and title and sending them from his email address. In dismissing the import of this

evidence, the Circuit Court reasoned only that this "sort of signature line . . . can often exist when one person sends an email that 'publishes a statement on behalf of another,' with the latter person retaining 'ultimate authority over the statement.'" *Lorenzo*, 872 F.3d at 588 (quoting *Janus*, 564 U.S. at 142, 131 S. Ct. 2296). This reasoning is flawed. As an initial matter, there is no evidence in the record upon which the Circuit Court based its observation regarding the nature of Lorenzo's signature line, or what the signature line signified for either Lorenzo or the recipients of his email.[5] To the contrary, had Lorenzo wanted to make it clear he was "publish[ing] a statement on behalf of" his bosses, *Lorenzo*, 872 F.3d at 588, he would have employed the commonly-used "sent on behalf of" function commonly used on Microsoft Outlook and other major email platforms.[6] That instead he affixed his own signature to the email and sent it from his account is dispositive.

The Circuit Court's reasoning is also flawed because it relies on language from *Janus* divorced from its context. In *Janus*, the Court held that, because the defendant was a "legally independent entity," it could not be the "maker" of a statement filed

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[5] Nor did the Circuit Court explain from whose perspective a court should determine the significance of the signature: a reasonable investor, the investor receiving the email, Lorenzo himself, or Gregg Lorenzo.

[6] *See Manage Another Person's Mail and Calendar Items*, Microsoft, https://support.office.com/en-us/article/manage-another-person-s-mail-and-calendar-items-afb79d6b-2967-43b9-a944-a6b953190af5.

with the SEC because it could not legally have the ultimate authority to file the statement with the SEC. 564 U.S. at 146-47, 131 S. Ct. 2296. Here, by contrast, there is no legally independent entity at issue; Lorenzo was a registered broker and director of investment banking at Charles Vista, LLC, with his own independent duties to that company and its investors. He could, and did, make statements that legally bound his company.

The Circuit Court's reasoning also appears to assume that only one individual within an organization can "make" a statement; that is, the Circuit Court assumed that if Gregg Lorenzo had "ultimate authority" over the email statements, Lorenzo cannot also have "ultimate authority" over the email statements. But there is no legal principle that limits Rule 10b-5(b) in such a manner. To the contrary, both SEC enforcement actions and private suits under Rule 10b-5(b) hold accountable multiple senior executives who, for instance, all signed a company's SEC filings containing untrue statements or all participated in an earnings conference call during which untrue statements were made. *See, e.g.*, *Waggoner v. Barclays PLC*, 875 F.3d 79 (2d Cir. 2017) (affirming class certification in Section 10(b) action against Barclays and three of its senior executives based on misstatements in, among other things, press releases); *In re Harman Int'l Indus., Inc. Sec. Litig.*, 791 F.3d 90 (D.C. Cir. 2015) (reversing and remanding dismissal of Section 10(b) claims against company and "three of its officers" for false statements made in the company's fiscal year 2007

Annual Report); *In re VeriFone Holdings, Inc. Sec. Litig.*, 704 F.3d 694 (9th Cir. 2012) (complaint adequately stated Section 10(b) claim against company, its CEO, and its CFO based on misstatements in SEC filing); *SEC v. Infinity Grp. Co.*, 212 F.3d 180 (3d Cir. 2000) (Alito, J.) (in Ponzi scheme case, upholding permanent injunction under Section 10(b) against company and its two principals). It is thus clear that, unlike in *Janus*, which dealt with a separate corporate entity, "*within an organization*, more than one person will have ultimate authority over a statement . . . ." *In re Barrick Gold Sec. Litig.*, No. 13 Civ. 3851(SAS), 2015 WL 3486045, at *2 (S.D.N.Y. June 2, 2015); *see also Banco Bradesco*, 277 F. Supp. 3d at 639 ("[N]othing in *Janus* dictates that only one person may have ultimate authority over a statement."); *City of Pontiac Gen. Emps.' Ret. Sys. v. Lockheed Martin Corp.*, 875 F. Supp. 2d 359, 374 (S.D.N.Y. 2012) ("It is not inconsistent with *Janus Capital* to presume that multiple people in a single corporation have the joint authority to 'make' an SEC filing, such that a misstatement has more than one 'maker.'")

If allowed to stand, the Circuit Court's implicit holding that only one individual within an organization can have "ultimate authority" would eviscerate Rule 10b-5(b) by allowing culpable individuals to escape liability. Take the following scenario: the CEO of a company orders her CFO to insert new language in the company's SEC filing, believing the language to be true. The CFO, knowing the language to be false, nevertheless inserts the new

language, and the CEO and CFO both sign the document and file it with the SEC. Under the Circuit Court's reasoning, neither of these executives would face liability under Rule 10b-5(b). The CFO could simply aver that she did not have "ultimate authority" over the statements because she acted at the direction of the CEO and copied-and-pasted the language the CEO provided to her, while the CEO could claim she lacked scienter. This illogical outcome underscores that the Circuit Court's interpretation stretches *Janus*'s concept of "ultimate authority" too far.

That Lorenzo's emails stated he was sending them "at the request of" his boss does not change this analysis. In addition to signing and sending the emails from his account, Lorenzo demonstrated his ultimate authority over the emails by reassuring investors that they could call *him* "with any questions" regarding the contents of the email or the nature of the investment. Moreover, because Lorenzo testified that he understood he was "putting his own reputation on the line" by sending the emails, there is strong evidence to support that Lorenzo would "take[] credit—or blame—for what [was] ultimately said," *Janus*, 564 U.S. at 143, 131 S. Ct. 2296.

In sum, just as a corporate executive is a "maker" of an untrue statement in a filing he signs, Lorenzo is a "maker" of the solicitation emails he chose to sign and send from his email account. It is thus appropriate to hold him liable under Rule 10b-5(b).

III. THE SAME ANALYSIS HEREIN APPLIES UNDER SECTION 17(A) OF THE SECURITIES ACT.

For the same reasons the Circuit Court upheld the Commission's scheme liability findings against Petitioner, the Circuit Court also affirmed the Commission's finding of liability under Section 17(a)(1) of the Securities Act of 1933, 15 U.S.C. § 77q(a)(1). *See Lorenzo*, 872 F.3d at 586. The Circuit Court was right to do so.

Rule 10b-5 is drafted substantially similarly to Section 17(a), and courts interpret liability under these provisions to be substantially similar. *SEC v. Radius Capital Corp.*, 653 Fed. Appx. 744, 749 (11th Cir. 2016). There is no reason to depart from this general principle here. The primary distinction between liability under Section 10(b) and Rule 10b-5 thereunder and Section 17(a) is that "§ 10(b) and Rule 10b-5 applies to acts committed in connection with a *purchase or sale* of securities while § 17(a) applies to acts in connection with an *offer or sale* of securities." *SEC v. Bauer*, 723 F.3d 758, 768 (7th Cir. 2013) (emphasis in original). This difference is of no moment here. Also of no consequence here are the distinctions in how scienter is treated under Section 10(b) and Section 17(a), and that there is no private right of action under Section 17(a). *See Radius Capital*, 653 Fed. Appx. at 749; *Finkel v. Stratton Corp.*, 962 F.2d 169, 170 (2d Cir. 1992)).

Similarly, for the reasons outlined above in Part II that Petitioner should be held liable under

Rule 10b-5(b) as the "maker" of the misleading emails he sent to prospective investors, it follows that he violated Section 17(a)(2) as well. Indeed, Section 17(a)(2) is even broader than Rule 10b-5(b): 17(a)(2) makes it unlawful to "obtain money or property *by means of*" any material misrepresentation or omission while 10b-5(b) requires the defendant to actually "make" the misstatement. *Compare* 15 U.S.C. § 77q(a)(2) *with* 17 C.F.R. § 240.10b-5(b)(2). Thus, to the extent a trier of fact were to find Petitioner liable under Rule 10b-5(b), corresponding liability logically follows under Section 17(a)(2).[7]

IV. THE SEC IS NOT ACTING IN BAD FAITH

The Professors' Brief criticizes the Commission's interpretation of the law with respect to primary versus secondary liability. The Professors' Brief asserts that the Commission "prefers primary fraud charges" and sees the limitations imposed by *Janus* as "a nuisance to avoid." *See* Professors' Brief at 6, 9. The Professors' Brief accuses the Commission further of seeking to "smudge the line" between primary and secondary liability as drawn by this Court. *See* Professors' Brief at 7. It is unclear whether the professors are accusing the Commission of bad faith in its interpretation of primary versus secondary liability, but their brief certainly suggests

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[7] The extent to which *Janus* even applies to Section 17(a)(2) is not settled. *Compare Big Apple*, 783 F.3d at 797 (holding *Janus* does not apply to claims under Section 17(a)(2)), *with SEC v. Knight*, 694 Fed. Appx. 853, 856 n.1 (2d Cir. 2017) (declining to reach the question). This issue need not be reached here.

as much. To the extent they do hold this view, we vigorously disagree.

The Commission has never, to our knowledge, asserted that it is not bound by *Janus*. If the Commission really were of a mind to pursue every legal theory as aggressively as possible, it could have challenged that *Janus's* holding about the scope of primary liability under Rule 10b-5(b) was inapplicable to its own enforcement actions. After all, *Janus* was a private litigation and the decision pointedly did not speak to its potential applicability to governmental actions. *See Janus*, 564 U.S. at 137 ("This case requires us to determine whether Janus Capital Management . . . can be held liable in a private action under [Rule 10b-5].") At least one SEC staff member after *Janus* publicly questioned whether the decision should apply to the agency's actions, *see* Yin Wilczek, *Extent to Which Janus Applies to SEC Actions Not Clear, Official Says*, 44 Sec. Reg. & L. Rep. (BNA) 462 (Mar. 5, 2012), and reasonable arguments can be made that *Janus* should not bind the SEC. *See* Matthew P. Wynne, Student Note, *Rule 10b-5(b) Enforcement Actions in Light of Janus: Making the Case for Agency Deference*, 81 FORDHAM L. REV. 2111 (2013). Yet the Commission has never contested this point. Rather, the inherent logic within *Janus* and the need for consistency across public and private litigations appears to have caused the Commission to forego this potential fight.

V. SIFMA AND THE CHAMBER'S HYPERBOLIC CLAIMS ARE MERITLESS

SIFMA and the Chamber argue that, if the Circuit Court's decision is sustained, one would become liable under Section 10(b) merely by playing some remote role in the dissemination of a statement. SIFMA/Chamber Brief at 14. They write further:

> Securities industry professionals, in particular, distribute the statements of others to their clients by many different channels and involving varying degrees of directness, including public and private websites, individual and mass emails, and the mailing or physical distribution of prospectuses. *Janus* clarified that they do not accept exposure to Section 10(b) or Rule 10b-5 liability each time they do so.

Id. These concerns are meritless hyperbole.

Securities professionals do not become liable for merely delivering prospectuses or other corporate disclosure documents as required by the securities laws and related rules. Rather, one is liable under Section 10(b) and Rule 10b-5 only for knowingly or recklessly distributing false and misleading information in order to effectuate the sale of a security (particularly a security the broker-dealer is itself underwriting).

Moreover, contrary to SIFMA/Chamber's supposition that an avalanche of meritless private litigation will be filed against security market actors

if the Circuit Court's decision is not reversed (*see id.* at 24-26), both the Private Securities Litigation Reform Act ("PSLRA"), Pub. L. No. 104-67, 109 Stat. 737 (1996), and the Securities Litigation Uniform Standards Act ("SLUSA"), Pub. L. No. 105-353, 112 Stat. 3227 (1998), as well as the Court's recent jurisprudence provide significant and ample protection against such suits. It is telling that neither petition nor *Amicus* can point to a single securities case filed against security market actors for distributing prospectuses or other routine acts.

It is essential that adequate remedies exist to protect hardworking investors impacted by fraud. Private securities litigation is a necessary supplement to SEC enforcement actions. *See Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 313 (2007)("[The Court] has long recognized that meritorious private actions to enforce federal antifraud securities laws are an essential supplement to criminal prosecutions and civil enforcement actions brought, respectively, by the Department of Justice and the Securities and Exchange Commission."); *Bateman Eichler, Hill Richards, Inc. v. Berner*, 472 U.S. 299, 310 (1985); *J.I. Case Co. v. Borak*, 377 U.S. 426, 432 (1964) (private rights of action under the securities laws are a "necessary supplement to Commission action."). As Commissioner Jackson explained earlier this year:

> "...[T]here are two principal ways we hold corporate managers to account when they hurt investors. First, the government can identify the wrongdoing and bring a case.

> Second, investors themselves can bring a lawsuit against the responsible individuals and companies. Government enforcement is crucial to the functioning of our securities markets . . . At the same time, I'm struck again and again by the sheer audacity of fraudsters and by the devastating amount of money investors lose. Almost daily, I am reminded that [the SEC's] world-class enforcement attorneys cannot do it all alone."[8]

Indeed, the amount of securities fraud is simply too great for the SEC and NASAA's members to police on their own. According to former SEC Chair Mary Jo White, "additional funding [for the SEC] is imperative if we are to continue the agency's progress in fulfilling its responsibilities over our increasingly fast, complex, and growing markets."[9] But Congressional budget authorizations have not kept

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[8] Commissioner Robert J. Jackson Jr., Keeping Shareholders on the Beat: A Call for a Considered Conversation About Mandatory Arbitration, CECP CEO Investor Forum, February 26, 2018, *available at* https://www.sec.gov/news/speech/jackson-shareholders-conversation-about-mandatory-arbitration-022618. *See also* NYU Pollack Center for Law and Business & Cornerstone Research, SEC Enforcement Activity: Public Companies and Subsidiaries, (November 14, 2017), https://www.cornerstone.com/Publications/Reports/SEC-Enforcement-Activity-Public-Companies-and-Subsidiaries-Midyear-FY-2018-Update ("[t]he number of new [SEC] actions [against public-company related defendants] declined 33 percent overall in FY 2017.").

[9] Mary Jo White, Testimony on the Fiscal Year 2017 Budget Request of the U.S. Securities and Exchange Commission (March 22, 2016), *available at* www.sec.gov/news/testimony/testimony-white-sec-fy-2017-budget-request.html.

pace with the SEC's needs.[10] State securities regulators face similar budgetary constraints.

Private securities litigation is also the primary mechanism for compensating harmed investors. While the funds obtained by federal and state regulators can in some cases be returned to identifiable investors, the amounts collected in governmental actions pale in comparison to the awards obtained by private litigants themselves. *See* John C. Coffee, Jr., *Reforming the Securities Class Action: An Essay on Deterrence and its Implementation*, 106 COLUM. L. REV. 1534, 1542-43 Tables 2 & 3 (2006). ("private enforcement . . . dwarf[s] public enforcement"). In 2016, roughly sixty cents of every dollar returned to investors in corporate-fraud cases came through private, rather than SEC, settlements.[11]

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[10] *See* Melanie Waddell, SEC Seeks Budget Boost to Restore Staff, ThinkAdvisor (February 12, 2018), available at https://www.thinkadvisor.com/2018/02/12/sec-seeks-budget-boost-to-restore-staff/?slreturn=20180911131549 ("The [SEC's] annual appropriations has remained essentially flat from 2016 to 2018, at $1.6 billion. However, during the same period, securities trading has grown by more than $3 trillion, assets under management by investment advisors has jumped more than $5 trillion, and there's been a 17% growth in ETFs and mutual funds.").

[11] *Compare* Cornerstone Research, Securities Class Action Settlements: 2016 Review and Analysis (2016) (noting that, in 2016, federal courts approved approximately $6 billion in securities class-action settlements); *with* U.S. Securities and Exchange Commission, SEC Announces Enforcement Results for FY 2016, Press Release, (Oct. 11, 2016) (noting that the SEC obtained just over $4 billion in disgorgement and penalties in FY 2016).

Private securities litigation also serves a significant role in maintaining investor confidence by enforcing disclosure standards set forth in the securities laws. As this Court has recognized, "[t]he magnitude of the federal interest in protecting the integrity and efficient operation of the market for nationally traded securities cannot be overstated." *Merrill Lynch, Pierce, Fenner & Smith Inc. v. Dabit*, 547 U.S. 71, 78 (2006). And, scholars have observed that investor lawsuits are as good, if not better, than the government in targeting certain securities-law violations.[12]

Congress too recognizes the important role played by private securities litigation in deterring fraud and compensating victims: "[t]he SEC enforcement program and the availability of private rights of action together provide a means for defrauded investors to recover damages and a powerful deterrent against violations of the securities laws." S. Rep. No. 98, 104th Cong. 1st Sess., at 8 (1995). And Congress recognizes the important role such actions play in maintaining investor confidence and ensuring market integrity:

> Private securities litigation is an indispensable tool with which defrauded investors can recover their losses without having to rely upon government action.

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[12] Stephen Choi & Adam Prichard, SEC Investigations and Securities Class Actions: An Empirical Comparison, 13 J. Emp. Legal Stud. 27 (2016).

> Such private lawsuits promote public and global confidence in our capital markets and help to deter wrongdoing and to guarantee that corporate officers, auditors, directors, lawyers and others properly perform their jobs.

H.R. CONF. REP. NO. 369, 104th Cong. 1st Sess. (1995), at 31 (Nov. 28, 1995).

Even in light of recent limitations placed on private actions by Congress, the underlying intent of Congress to allow for these remedies remains. Congress recognizes the importance of private actions to the overall functioning of the securities markets. To the extent there may be any concerns about the process for which private securities litigations, these concerns are "more appropriately addressed by Congress," not this Court. *Halliburton Co. v. Erica P. John Fund*, 134 S. Ct. 2398, 2413 (2014).

CONCLUSION

For all of the foregoing reasons, we respectfully submit that Petitioner should be held in violation of Securities Exchange Act of 1934 Section 10(b) and Rule 10b-5(a), (b), and (c) promulgated thereunder, as well as Section 17(a)(1), (2) and (3) of the Securities Act of 1933.

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IN THE

Supreme Court of the United States

FRANCIS V. LORENZO,

Petitioner,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

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INTEREST OF *AMICI CURIAE*[1]

The Securities Industry and Financial Markets Association ("SIFMA") is the leading trade association for broker-dealers, investment banks and asset managers operating in the U.S. and global capital markets. On behalf of the industry's nearly 1 million employees, SIFMA advocates on legislation, regulation and business policy, affecting retail and institutional investors, equity and fixed income markets and related products and services. SIFMA serves as an industry coordinating body to promote fair and orderly markets, informed regulatory compliance, and efficient market operations and resiliency. It also provides a forum for industry policy and professional development. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit http://www.sifma.org.

The Chamber of Commerce of the United States of America ("Chamber") is the world's largest business federation. It represents 300,000 direct members and indirectly represents the interests of more than 3 million companies and professional organizations of every size, in every industry sector, and from every region of the country. An important function of the Chamber is to represent the interests of its members in matters before Congress, the Executive Branch, and the courts. To that end, the Chamber regularly files *amicus curiae*

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[1] Pursuant to Rule 37.6, SIFMA and the Chamber confirm that no counsel for a party authored this brief in whole or in part and that no person other than SIFMA or the Chamber, their members, or their counsel made a monetary contribution intended to fund the preparation or submission of this brief. Pursuant to Rule 37.3(a), the parties have consented to the filing of this brief, each in a separate writing filed concurrently with this brief.

briefs in cases such as this one that raise issues of concern to the nation's business community.

SIFMA and Chamber members and their directors, officers, and employees are often subjected to civil suits or Commission enforcement actions brought under Section 10(b) of the Exchange Act of 1934 and Rule 10b-5. Civil litigation brought in pursuit of damages, in particular, imposes enormous burdens, including disruption of business, litigation costs, and settlement expenses. Enforcement actions brought by the government add the prospect of sanctions that can end an individual's career or criminal penalties that can include incarceration. SIFMA and the Chamber, and the businesses and individuals whose interests they represent, thus have a keen interest in obtaining clear guidance regarding when Section 10(b) and Rule 10b-5 liability may attach.

SUMMARY OF THE ARGUMENT

In *Janus Capital Group, Inc.* v. *First Derivative Traders*, this Court held that one person *cannot* be "held liable . . . under Rule 10b-5 for false statements" made by another. 564 U.S. 135, 141 (2011). Now, just seven years later, the D.C. Circuit has held that petitioner Francis Lorenzo *can* be held liable for false statements made by another (Lorenzo's boss), reasoning that this contrary result is warranted because its decision rests on subsections (a) and (c) of Rule 10b-5, whereas *Janus* supposedly addressed only subsection (b) of that Rule.

This Court should reverse and make clear that there is no liability in these circumstances under Rule 10b-5 regardless of the subsection involved. "For purposes of Rule 10b-5," *as a whole*, "the maker of a statement is the person or entity with ultimate authority over the

statement, including its content and whether and how to communicate it." *Id.* at 142. That is the only answer consistent with the controlling statute—Section 10(b)—and with the Court's decisions construing that statute, including *Janus*.

I.A. The D.C. Circuit's key error was its myopic reliance on the language of *the regulation*, Rule 10b-5(a) and (c), to the exclusion of any meaningful analysis of whether Lorenzo's conduct violated *the statute*, Section 10(b). This Court's precedents instead command a statute-focused approach.

A "complaint states a cause of action under *any part of Rule 10b-5* only if the conduct alleged can be fairly viewed as 'manipulative or deceptive' within the meaning of the statute." *Santa Fe Indus., Inc.* v. *Green*, 430 U.S. 462, 473–74 (1977) (emphasis added). However broad the language of Rule 10b-5, "its scope cannot exceed the power granted the Commission by Congress under § 10(b)." *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 214 (1976). That insight reverberates throughout the Court's Section 10(b) cases, several of which have refused to find liability in circumstances covered by the text of Rule 10b-5, but not Section 10(b). See *Ernst*, 425 U.S. at 212–14; *Aaron* v. *SEC*, 446 U.S. 680, 691 (1980); *Chiarella* v. *United States*, 445 U.S. 222, 225–26 (1980).[2]

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[2] The Court's approach reflects in part the fact that Rule 10b-5 was released with only an afternoon's worth of thought and a single sentence of explanation. Indeed, the Commission essentially created the Rule by copying the language of a different statute (Section 17(a) of the 1933 Act) and pasting it into its regulation as an interpretation of Section 10(b). *See Ernst*, 425 U.S. at 212 n.32.; 1 Louis Loss, Joel Seligman & Troy Paredes, Securities Regulation 9.B.3 (5th ed. 2013).

In light of Section 10(b)'s primacy, the Court's decisions have been careful to define the categories of conduct that violate Section 10(b)'s proscription of the "use or employ[ment] of "any manipulative or deceptive device" in connection with the purchase or sale of securities. See 15 U.S.C. § 78j(b). In *Central Bank of Denver, N.A.* v. *First Interstate Bank of Denver, N.A.*, the Court summarized those decisions, stating pointedly that the statute "prohibits *only* the *making* of a material misstatement (or omission) or the *commission* of a manipulative act." 511 U.S. 164, 175, 177–78 (1994) (emphases added). More recently, the Court's decision in *Stoneridge Investment Partners, LLC* v. *Scientific-Atlanta*, 552 U.S. 148, 158 (2008), reiterated that Section 10(b) violations consist of "only misstatements, omissions by one who has a duty to disclose, and manipulative trading practices (where 'manipulative' is a term of art)" (citation omitted).

Seeking to create stable and predictable zones of liability, the Court has also carefully cabined the scope of each category of Section 10(b) violations. In *Santa Fe*, the Court confined "manipulation" to certain trading practices "that are intended to mislead investors by artificially affecting market activity." 430 U.S. at 476. With respect to the duty to disclose, the Court repeatedly has held that a non-speaking defendant (such as an inside trader) may violate Section 10(b) only by violating a duty of disclosure grounded in a relationship of trust and confidence. See, *e.g.*, *Dirks* v. *SEC*, 463 U.S. 646, 653–55, 657–59 (1983). Then, in *Janus*, the Court addressed the last category of Section 10(b) violations, clarifying that, in defining the prohibition on "the making of a material misstatement," *Cent. Bank*, 511 U.S. at 177, it would "not expand liability beyond the person or entity that ultimately has authority over a false statement." *Janus*, 564 U.S. at 144.

B. Reading the liability rule in *Janus* as applying to Section 10(b) is the only sensible way of reconciling this Court's longstanding precedents, in an area where clear, predictable rules and considerations of *stare decisis* are especially pronounced. The contrary rule sought by the Commission and embraced by the D.C. Circuit would dramatically blur long-settled lines between speaker and non-speaker liability under Section 10(b), and would "erase the line between primary violators and aiders and abettors established by *Central Bank*." *Janus*, 564 U.S. at 143, 147 & n.11.

It would also rob Rule 10b-5(b) of all meaning. In the Commission's view (which the D.C. Circuit adopted), "primary liability under Rule 10b-5(a) and (c) *also* encompasses the 'making' of a fraudulent misstatement to investors"—just like primary liability under Rule 10b-5(b). See *Matter of John P. Flannery & James D. Hopkins*, Release No. 3981, at *12 (Dec. 15, 2014), *rev'd on other grounds*, *Flannery* v. *SEC*, 810 F.3d 1 (1st Cir. 2015). This interpretation would reduce Rule 10b-5(b) to surplusage, even while *also* abrogating, in practical effect, the limitation on liability set out in *Janus*. That is no way to read a regulatory text, or an opinion of this Court for that matter.

C. The construction of Section 10(b) and Rule 10b-5 proposed by *amici*, in contrast, would respect the Court's Section 10(b) precedents and the structure of Rule 10b-5. It would also give due regard to the 1933 and 1934 Acts. These statutes contain numerous provisions that expressly impose liability—albeit in carefully circumscribed ways—for the same kind of secondary uses of misstatements that the D.C. Circuit held are implicitly prohibited by Rule 10b-5(a) and (c). These provisions reach those who "cause" or "control" the making of misstatements; "willfully participate[]" in certain misstatements; sell securities "by means of"

documents containing misstatements; or (of particular relevance here) "publish, give publicity to, or circulate"; or "disseminat[e]" certain misleading documents.

D. Finally, grounding *Janus* firmly in Section 10(b) would bring clarity and stability to the securities laws and therefore to the securities markets. Uncertain rules not only are unfair to public enforcement respondents like Lorenzo, they create fodder for abusive private suits. These suits make the country's public capital markets less attractive to entrepreneurs, which shifts investment towards private equity. A decision from this Court that reaffirms the clear and workable liability rule recognized in *Janus* would accordingly accrue to the benefit of the investing public.

II. In addition to reversing the Section 10(b) portion of the decision below, the Court should vacate and remand to the D.C. Circuit the Section 17(a)(1) charge. The D.C. Circuit treated Section 17(a)(1) as condemning the same behavior that Rule 10b-5(a) and (c) prohibit. But as demonstrated, Section 10(b), and thus Rule 10b-5, does not reach Lorenzo's conduct, and it is not clear what the D.C. Circuit would have held regarding Section 17(a)(1) had it separately analyzed that provision. Moreover, the courts of appeals have not significantly addressed Section 17(a)(1)'s proper scope, and because the Commission charged Lorenzo with employing an unlawful "device" or "artifice," but not an unlawful "scheme," this case does not present the Court with an opportunity to consider the full reach of Section 17(a)(1)—let alone the relationship of that provision to other provisions of Section 17. *Amici* respectfully submit, therefore, that the Court can and should decide this case without opining on whether Lorenzo violated Section 17(a)(1).

ARGUMENT

I. THE D.C. CIRCUIT ERRED BY FAILING TO INTERPRET RULE 10b-5 IN LIGHT OF ESTABLISHED LIMITATIONS ON SECTION 10(b) LIABILITY.

The D.C. Circuit erred when it ignored this Court's many decisions delimiting Section 10(b) and Rule 10b-5 as a whole. *Janus* followed from those decisions. The Court should confirm that the rule of *Janus*—including its approach to attribution, adoption, and dissemination—applies to any claim brought under Section 10(b) and Rule 10b-5 that is founded solely on an alleged misstatement. This rule would preserve the important distinction between primary and secondary violators and between potential liability for speaking and non-speaking defendants, give proper effect to other provisions of the securities laws, and protect the nation's public capital markets against the threat of unwarranted private and public enforcement actions.

A. Section 10(b) Governs The Scope Of Liability Under Rule 10b-5 And Proscribes Only Certain Well-Defined Conduct.

1. The Court long ago held that Rule 10b-5 does not reach any conduct outside the four corners of the Rule's authorizing statute, Section 10(b) of the 1934 Act. In *Ernst*, the Commission claimed authority to prosecute negligent behavior under Rule 10b-5, arguing that the broad language of Rule 10b-5(b) and (c) "standing alone could encompass . . . negligent behavior." 425 U.S. at 212. The Court agreed that the Rule's language alone "could be read as proscribing . . . any course of conduct, that has the effect of defrauding investors, whether the wrongdoing was intentional or not." *Id.*

The Court, however, rejected the Commission's invitation to read the regulation in isolation. It held that, "despite the broad view of [Rule 10b-5] advanced by the Commission," the Rule's "scope cannot exceed the power granted the Commission by Congress under [Section] 10(b)." *Id.* at 214. This holding followed from basic tenets of administrative law: the "rulemaking power granted to an administrative agency . . . is not the power to make law." *Id.* at 213. An agency only has "the power to adopt regulations to carry into effect the will of Congress as expressed by the statute." *Id.* at 214 (quoting *Dixon* v. *United States*, 381 U.S. 68, 74 (1965)).

After holding that Section 10(b) demarcated the potential reach of Rule 10b-5, the Court determined that the Commission's reading of Rule 10b-5 exceeded those bounds. Drawing from Section 10(b)'s reference to "manipulation and deception, and of implementing devices and contrivances," *id.* at 214, the Court held that Rule 10b-5 could not be construed to reach negligent conduct—even if the language of the Rule itself went that far. *Id.*

Despite the Court's reliance in *Ernst* on the statutory text, the Commission tried to limit *Ernst* to the judicially implied private right of action. In *Aaron* v. *SEC*, the Commission argued that the rule adopted in *Ernst* applied only to private Rule 10b-5 suits, not to injunctive actions brought by the Commission. 446 U.S. at 689. The Court rejected this attempt to artificially limit *Ernst*'s reading of the statute, and squarely held that regardless whether an action is brought by a private plaintiff or the Commission, "the language of § 10(b)" controls the scope of liability under Rule 10b-5. *Id.* at 694–95.

2. Having established the primacy of Section 10(b), the Court has since delineated the conduct the statute prohibits. Section 10(b) only prohibits the "use" or "employ[ment]" of "any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe." 15 U.S.C. § 78j(b). The Court has homed in on the statute's "deceptive" or "manipulative" qualifiers, holding that a "complaint states a cause of action under *any part of Rule 10b-5* only if the conduct alleged can be fairly viewed as 'manipulative or deceptive' within the meaning of the statute." *Santa Fe*, 430 U.S. at 473–74 (emphasis added).

In *Santa Fe*, a parent company had relied on a Delaware corporate law provision permitting the company to buy out minority shareholders in exchange for cash. *Id.* at 465–68. The plaintiffs attempted to assert liability based on the broad language of Rule 10b-5(a) and (c), alleging that the defendants had engaged in a "device, scheme, or artifice to defraud," through a "gross undervaluation" of the plaintiffs' shares, in breach of their fiduciary duty to the plaintiffs. *Id.* at 467–68.

The Court disagreed. The Court first noted that the defendants had not engaged in any "deceptive" act under Section 10(b) since the plaintiffs did not allege a "material misrepresentation or material failure to disclose." *Id.* at 474. That the defendants allegedly had breached their fiduciary duty was not enough—absent a misstatement by the defendants, the defendants' conduct, however inappropriate or distasteful, did not constitute the "deception" that Section 10(b) prohibits. *Id.* at 474–75. As to manipulation, the Court held it "readily apparent" that the defendants' actions were "not 'manipulative' within the meaning of the statute." *Id.* at 476. As the Court explained, "'[m]anipulation' is

'virtually a term of art when used in connection with securities markets.'" *Id.* (quoting *Ernst*, 425 U.S. at 199). "The term refers generally to practices, such as wash sales, matched orders, or rigged prices, that are intended to mislead investors by artificially affecting market activity." *Id.*

A few years later, the Court returned to the scope of "deceptive," as that term is used in Section 10(b). In *Chiarella* v. *United States*, the defendant was charged with a criminal violation of Section 10(b), on the theory that he had unfairly traded on material non-public information. 445 U.S. at 224–25. The jury instruction tracked the broad language of Rule 10b-5 subsections (a) and (c): the jury could convict the defendant if it found that he "employed a device, scheme, or artifice to defraud" or "engaged in an act, practice, or course of business which operated or would operate as a fraud or deceit upon any person." *Id.* at 236.[3]

This Court reversed. It held that the defendant did not do anything "deceptive" within the meaning of Section 10(b) because "there can be no fraud absent a duty to speak," and on the facts before the Court, the defendant had no such specific duty. *Id.* at 235. In so ruling, the Court also rejected the Second Circuit's suggestion that *anyone* possessing superior market information has a "general duty" running to "all participants in market transactions," *Chiarella*, 445 U.S. at 233, to disclose that information (or refrain from trading on it) regardless of any pre-existing relationship. See *United States* v. *Chiarella*, 588 F.2d 1358, 1364–

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[3] The government's indictment also invoked the misstatement language of Rule 10b-5(b). However, that portion of its indictment was dismissed since Chiarella had not made any affirmative statement. *Chiarella*, 445 U.S. at 225 n.5.

66 (2d Cir. 1978). The Court found no basis in the statute to support such a sweeping duty and cautioned that, "[a]s we have emphasized before, the 1934 Act cannot be read 'more broadly than its language and the statutory scheme reasonably permit.' . . . Section 10(b) is aptly described as a catchall provision, but what it catches must be fraud." *Chiarella*, 445 U.S. at 234–35 (quoting *Touche Ross & Co.* v. *Redington*, 442 U.S. 560, 578 (1979); *SEC* v. *Sloan*, 436 U.S. 103, 116 (1978)).[4]

The Court affirmed and restated all of these holdings in its 1994 *Central Bank* decision: "As in earlier cases considering conduct prohibited by § 10(b), *we again conclude that the statute prohibits only the making of a material misstatement (or omission)*," which can include a non-disclosure coupled with a duty to speak, "*or the commission of a manipulative act.*" 511 U.S. at 177–78 (emphases added). The Court then restated the same framework in its 2008 *Stoneridge* decision, confirming that Section 10(b) violations consist of "only

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[4] The Court relied both on its prior common law and Section 10(b) precedents and on the Commission's own *Cady, Roberts* decision to conclude that "such liability is premised upon a duty to disclose arising from a relationship of trust and confidence between parties to a transaction." *Chiarella*, 445 U.S. 226–30 (citing *Matter of Cady, Roberts & Co.*, 40 S.E.C. 907, 911–13 (Nov. 8, 1961)). The Court, moreover, has since repeatedly adhered to *Chiarella*'s duty framework to define deceptive conduct under Section 10(b). *See, e.g., United States* v. *O'Hagan*, 521 U.S. 642, 654–55 (1997) ("Because the deception . . . involves feigning fidelity to the source of information, if the fiduciary discloses to the source that he plans to trade on the nonpublic information, there is no 'deceptive device' and thus no § 10(b) violation"); *SEC* v. *Zandford*, 535 U.S. 813, 821–23, 825 n.4 (2002) (broker's Rule 10b-5(a) and (c) liability for misappropriating assets derived from failure to make disclosure required by fiduciary duty arising from discretion over client investments); *see also Salman* v. *United States*, 137 S. Ct. 420, 423 (2016); *Dirks*, 463 U.S. at 653–55, 657–59.

misstatements, omissions by one who has a duty to disclose, and manipulative trading practices (where 'manipulative' is a term of art)." 552 U.S. at 158 (citation omitted).

To be sure, there can be liability under Section 10(b) *without* an "oral or written statement" because "[c]onduct itself can be deceptive." *Id.* But this only underscores rather than amends the rule laid out in this Court's precedents. "Deception" consists of misstatements (including misstatements conveyed through conduct rather than words), or the failure to disclose in light of a clearly established duty to do so. "Manipulation" consists of a defined set of conduct, as explained in *Santa Fe*. Those are the only bases for liability covered by Section 10(b), and thus the only bases that any provision of Rule 10b-5 can properly reach.

3. In light of this long tradition, the Court's *Janus* decision is properly understood as a case that refined the meaning of "deceptive" under Section 10(b) by addressing what it means to commit a "deceptive" act through "the making of a material misstatement or omission." *Cent. Bank*, 511 U.S. at 177.

In *Janus*, the Court began by stating the question presented in holistic terms, asking whether "a mutual fund investment adviser, can be held liable in a private action under Securities and Exchange Commission (SEC) *Rule 10b-5* for false statements included in its client mutual funds' prospectuses." 564 U.S. at 137 (emphasis added); see also *id.* at 141 (case concerned liability "under Rule 10b-5 for false statements"). The Court also emphasized that the Commission "promulgated Rule 10b-5 pursuant to authority granted under § 10(b) of the Securities Exchange Act of 1934." *Id.* at 141.

Of course, the Court also placed significant weight on the specific language of Rule 10b-5(b), *id.* at 142. But it would be a mistake to read *Janus* (as the Commission and D.C. Circuit have), as a decision addressed *solely* to misstatements liability under Rule 10b-5(b), and not to misstatements liability under Section 10(b) and Rule 10b-5 as a whole.

In fact, the Court was careful to note that the "rule" it announced "follow[ed] from" its decisions interpreting Section 10(b) and Rule 10b-5 such as *Central Bank*, *id.* at 143, and described that "rule" as applying "for purposes of Rule 10b-5"—not just subsection (b) of Rule 10b-5. *Id.* at 142, 148 & n.12. Moreover, the Court pointed out that this was "not the first time" it had "disagreed with the SEC's broad view of § 10(b) or Rule 10b–5" and cited *Central Bank*, *Dirks*, and *Ernst*, among other leading Section 10(b) precedents. *Id.* at 145 n.8. Finally, the Court twice noted that a broader reading would effectively expand primary liability to encompass aiders and abettors, contrary to *Central Bank* and *Stoneridge*. *Id.* at 143, 145. The Court's "rule" should thus be taken at face value as an interpretation of both Section 10(b) and Rule 10b-5. "[T]he maker of a statement is the entity [or person] with authority over the content of the statement and whether and how to communicate it." *Id.* at 144. No one other than a "maker" may be subjected to primary liability under Section 10(b) and Rule 10b-5 on the theory that the statement was materially false or misleading.

That conclusion is buttressed by *Janus*'s explicit holding that merely acting as a conduit in disseminating the statements of others is "not a basis for liability." *Id.* at 147–48 & nn.11–12 (rejecting argument that distributing a prospectus by hosting it on a company website gives rise to liability). The Court further explained that Rule 10b-5 does not impose liability for

making a statement "indirectly" unless the statement was "attributed, explicitly or implicitly, to" the defendant: "[m]ore may be required . . . but attribution is necessary." *Id.* at 147 n.11.

At the petition stage, the Commission obliquely referenced this aspect of *Janus* by arguing that the defendant in that case, unlike Lorenzo, "played no *active* role in disseminating the misstatements." BIO 14–15 (emphasis added). See also Pet. App. 21, 24–25. But the *Janus* standard does not turn on the role that a person or entity may play with respect to dissemination. To the contrary, *Janus* made clear that "[m]erely hosting a document on a Web site *does not* indicate that the hosting entity adopts the document as its own statement or exercises control over its content." 564 U.S. at 148 n.12 (emphasis added).

That one does not become civilly or criminally liable under Section 10(b) merely by playing some role in the dissemination of a statement is critical to *amici* and to the businesses and individuals whose interests they represent. Securities industry professionals, in particular, distribute the statements of others to their clients by many different channels and involving varying degrees of directness, including public and private websites, individual and mass emails, and the mailing or physical distribution of prospectuses. *Janus* clarified that they do not accept exposure to Section 10(b) or Rule 10b-5 liability each time they do so.

The *Janus* standard thus offers clear guidance, consistent with this Court's precedents, for when such activities require securities industry professionals to take responsibility for the contents of documents that they disseminate. That is a crucial consideration in an "'an area that demands certainty and predictability,'" *Cent. Bank*, 511 U.S. at 188 (quoting *Pinter* v. *Dahl*,

486 U.S. 622, 652 (1988)), and in which this Court has previously rejected tests that are "complex in formulation and unpredictable in application." *Morrison* v. *Nat'l Austl. Bank Ltd.*, 561 U.S. 247, 256 (2010). Neither the Commission nor the D.C. Circuit considered whether the tests they adopted would promote the certainty and predictability across cases that this Court has properly recognized as vital to the proper operation of the securities markets. *Amici* urge this Court to preserve and reaffirm the clear and consistent *Janus* rule.[5]

B. The D.C. Circuit's Approach Would Undermine Section 10(b)'s Limitations On Rule 10b-5 Liability.

1. The D.C. Circuit and the Commission gave far too little consideration to this Court's prior Section 10(b) decisions and to *Janus*'s place within that line of decisions. Indeed, in a 2014 opinion, the Commission went so far as to suggest that the Court had not defined "the meaning of 'deceptive'" devices or contrivances under Section 10(b). *Flannery*, Release No. 3981, at *12 & n.52. To the contrary, this Court's decisions set forth

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[5] The D.C. Circuit appeared to mix and match standards with its observation that Lorenzo had "effectively vouched for the emails' contents," which it described as "self-attributed communications sent directly to investors." Pet. App. 25. But it is apparently undisputed at this stage, as reflected in the question presented in both the Petition and the Commission's Opposition, that the D.C. Circuit correctly held that Lorenzo did not violate Rule 10b-5(b) under *Janus*. Pet. App. 15–19. Vouching or self-attribution were not the bases on which the Commission had found Rule 10b-5(a) or (c) liability. Pet. App. 77. Nor is the D.C. Circuit's offhand formulation consistent with the approach to attribution or adoption taken in *Janus*, which should be the proper analytical framework.

above have amply defined and delimited the "deceptive" conduct that Section 10(b) prohibits, and that Rule 10b-5 properly can reach.

Santa Fe and *Chiarella*—the Court's decisions interpreting Section 10(b)'s proscription of "deceptive" devices—make clear that Section 10(b) only reaches misstatements consisting of a "material misrepresentation or material failure to disclose" (in light of a duty to do so). *Santa Fe*, 430 U.S. at 474; *Chiarella*, 445 U.S. at 236. *Janus* clarified these earlier decisions, holding that misstatement liability attaches only to those responsible for its content.

It was thus error for the D.C. Circuit to say that involvement with a misstatement violates Rule 10b-5(a) and (c), based solely on the observation (accurate, so far as it goes) that those subsections are stated in broad terms. As discussed above, the primary question under this Court's Section 10(b) cases is whether the charged conduct violates *the statute*. Once the D.C. Circuit determined that Lorenzo did not "make" the false statements that formed the basis for the Commission's charges, that should have been the end of the inquiry, absent an allegation that Lorenzo violated Section 10(b) in another way recognized by the Court's case law (*i.e.*, by remaining silent where he had a duty to speak, or by engaging in "manipulation," within the meaning of that term of art). Because no other such basis for liability under Section 10(b) was found, the conclusion that Lorenzo did not "make" the charged misstatements means that he did not violate Section 10(b) or Rule 10b-5.

2. The D.C. Circuit also went wrong in attempting to downplay the conflict between its conclusion and a key animating rationale of the Court's decisions in *Janus* and *Central Bank*—to hold the Rule 10b-5 private right of action within properly "narrow dimensions."

Janus, 564 U.S. at 142 (quoting *Stoneridge*, 552 U.S. at 167).

In *Central Bank*, the Court held that "Rule 10b–5's private right of action does not include suits against aiders and abettors." *Id.* at 143. Following *Central Bank*, Congress amended the law to allow aiding and abetting claims to be brought, but only by the Commission, 15 U.S.C. § 78t(e), leaving that side door firmly shut to private litigants. That legislative choice has informed the Court's reasoning in subsequent Section 10(b) cases. In *Stoneridge*, the Court rejected the petitioner's "view of primary liability," since it would have made "any aider and abettor liable under § 10(b) if he or she committed a deceptive act in the process of providing assistance." 552 U.S. at 162. And in *Janus*, the Court reasoned that "[a] broader reading of 'make,' including persons or entities without ultimate control over the content of a statement, would substantially undermine *Central Bank*. If persons or entities without control over the content of a statement could be considered primary violators who 'made' the statement, then aiders and abettors would be almost nonexistent." 564 U.S. at 143.

The D.C. Circuit suggested that its holding could be squared with *Janus* because "Lorenzo himself communicated with investors" and "his involvement was transparent to them." Pet. App. 24–25. The flaw in that rationale should be apparent: aiders and abettors may act visibly, and often do, as this Court's Section 10(b) cases well illustrate. The investment adviser in *Janus* and the indenture trustee in *Central Bank* both had investor-facing roles that were visible to the plaintiffs in those cases. More broadly, conduct that qualifies as aiding and abetting is very often "transparent"—driving the getaway car is a quintessential example. See 2 Wayne R. LaFave, *Substantive Criminal*

Law § 13.2(a) (3d ed. 2017). And nothing in *Janus* or *Central Bank* or recent congressional enactments provides any ground for suggesting, as the D.C. Circuit did, that *some* aiders and abettors (the "visible" ones) may be treated as primary violators of Section 10(b).

Judge Kavanaugh put his finger on another aspect of this key issue in his dissenting opinion below. "For decades [] the SEC has tried to erase" the distinction between primary and secondary liability this Court has worked hard to maintain. Pet. App. 46–47; see also Andrew N. Vollmer, *SEC Revanchism and the Expansion of Primary Liability Under Section 17(a) and Rule 10b-5*, 10 VA. L. & Bus. Rev. 273, 275 (2016) ("much of *Flannery* is not consistent with, and is antagonistic to, a series of prominent Supreme Court decisions that imposed meaningful boundaries around aspects of primary liability under Rule 10b-5"). The court of appeals should not have countenanced the Commission's latest effort, and this Court certainly should not. It should instead hold that neither the Commission nor private litigants can evade the rule of *Janus* by relabeling misstatement claims as violations of Rule 10b-5 subsections (a) and (c). A person may not be subject to liability for a misstatement unless the misstatement is attributable to that person—merely sending an email, hosting a webpage, or otherwise being part of the chain of events that leads to the statement's distribution is not enough. To be liable under Section 10(b) and Rule 10b-5, the person must "make" the statement personally or clearly adopt it as his or her own.

3. The D.C. Circuit's holding also fails to make sense of the language and structure of Rule 10b-5 as a whole. Unlike subsection (b), neither subsections (a) nor (c) uses the word "statement." See 17 C.F.R. § 240.10b-5. Instead, subsection (a) speaks of "any device, scheme,

or artifice" and subsection (c) speaks of "any act, practice, or course of business." *Id.* These words do not connote speaking, writing, or otherwise communicating, and are hardly synonymous with making a "statement." Especially when they are juxtaposed onto subsection (b)'s express focus on "statement[s]," they are best read to be referring to conduct *other than* statements. Indeed, if subsection (a) and (c) embody all misstatement cases, then subsection (b) has no purpose or meaning at all—a result at odds with the established principle that courts should not read "text in a way that makes part of it redundant." See *Nat'l Ass'n of Home Builders* v. *Defs. of Wildlife*, 551 U.S. 644, 669 (2007).

By contrast, applying *Janus* to all Section 10(b) claims would leave plenty of work for Rules 10b-5(a) and (c). As noted above, while Rule 10b-5(b) addresses statements, it does not address omissions (except those that render a statement misleading), or market manipulation, or insider trading—all of which are Rule 10b-5(a) and (c) violations routinely charged by the Commission.

C. The D.C. Circuit's Interpretation Fails To Take Account Of Other Securities Law Provisions That Expressly Address Misuses Of Statements.

Applying the *Janus* rule to all misstatement cases under Section 10(b) would help give effect to Congress's careful allocation of responsibilities and liability across the securities laws. In particular, the Commission's effort to extend primary liability for merely assisting in the dissemination or circulation of a statement made by another runs up against the fact that Congress knew how to create liability for precisely that type of conduct, and expressly did so elsewhere in the 1933 and 1934 Acts.

Section 9(a)(5) of the 1934 Act. To take one prime example, Section 9(a)(5) of the 1934 Act makes it unlawful for anyone receiving consideration from certain market actors (such as selling broker-dealers) "to induce the purchase of any security . . . *by the circulation or dissemination of information* to the effect that the price of any such security will or is likely to rise or fall because of the market operations of any 1 or more persons" for that purpose. 15 U.S.C. § 78i(a)(5) (emphasis added). For another, Section 17(b) of the 1933 Act makes it unlawful in certain circumstances "to *publish, give publicity to, or circulate* any notice, circular, advertisement, newspaper, article, letter, investment service, or communication which, though not purporting to offer a security for sale, describes such security." *Id.* § 77q(b) (emphasis added).

More broadly, multiple provisions of the 1933 and 1934 Acts provide various avenues for liability for secondary involvement in statements, but subject to restrictions that do not apply to Section 10(b). These include Sections 9 and 18 of the 1934 Act, both of which this Court has long seen as "close in structure, purpose, and intent to the 10b-5 action," *Musick, Peeler & Garrett* v. *Employers Ins. of Wausau*, 508 U.S. 286, 295 (1993), and both of which "target the precise dangers that are the focus of § 10(b)," *id.* at 296 (quoting *Lampf, Pleva, Lipkind, Prupis & Petigrow* v. *Gilbertson*, 501 U.S. 350, 360 (1991)).

Section 9(f) of the 1934 Act. Section 9(f) of the 1934 Act, 15 U.S.C. § 78i(f), reaches beyond defendants who use or employ the specified unlawful devices. Sections 9(a)–(c) prohibit certain enumerated forms of market manipulation, *id.* § 78i(a)–(c), Section 9(a)(4) prohibits false or misleading statements by a dealer, broker, "or other person selling or offering [a security]

for sale" made "for the purpose of inducing the purchase or sale" of that security, *id.* § 78i(a)(4), and as noted above, Section 9(a)(5) prohibits circulating or disseminating certain information, *id.* § 78i(a)(5). Unlike Section 10(b), Section 9(f) creates additional express private civil liability for "[a]ny person who *willfully participates in* any act or transaction" prohibited by Sections 9(a)–(c). *Id.* § 78i(f) (emphasis added). As this Court has held, Section 9(f) shows that "Congress knew of the collateral participation concept," and thus that the concept should not be implied into other civil-liability provisions. *Pinter*, 486 U.S. at 650 n.26.

Section 18(a) of the 1934 Act. Section 18(a) imposes liability on any defendant who "shall make *or cause to be made*" a statement that is "false or misleading with respect to any material fact" in "any application, report or document filed" pursuant to the 1934 Act. 15 U.S.C. § 78r(a) (emphasis added). In Section 10(b), by contrast, Congress did not prohibit the "causing" of a deceptive device, but instead stopped at the defendant who actually "use[s] or employ[s]" the deceptive device in connection with a purchase or sale of securities.

Section 20(a) of the 1934 Act and § 15 of the 1933 Act. In Sections 20(a) of the 1934 Act, 15 U.S.C. § 78t(a), and Section 15(a) of the 1933 Act, 15 U.S.C. § 77o(a), Congress authorized liability against "control persons." These two statutes make a person who "controls" another liable "to the same extent" as the "controlled person." *Id.* §§ 77o(a), 78t(a). By reaching control persons, these statutes, "in marked contrast to the implied [Section] 10 remedy . . . impose derivative liability." *Musick, Peeler*, 508 U.S. at 296. There is no need to stretch Section 10(b) and Rule 10b-5 to do work that Congress has already done elsewhere and with greater precision.

Sections 11 and 12 of the 1933 Act. Section 11 of the 1933 Act creates a claim only against enumerated defendants for misrepresentations or omissions in a registration statement for an offering of new securities. See 15 U.S.C. § 77k(a). This list includes directors of the issuer, underwriters, and those who sign or consent to be named in a registration statement. *Id.* Section 12(a)(1) and (a)(2) claims are directed against anyone who "[o]ffers or sells a security . . . *by means of* a prospectus or oral communication" that is false or misleading, or in violation of registration requirements, and may be brought only by "the person purchasing such security from him." *Id.* § 77*l*(a)(1)–(2) (emphasis added). The class of defendants is limited to those in privity with the plaintiff or who directly solicit the plaintiff's purchase at least in part for their own financial gain. This Court rejected extending Section 12 liability further to someone "whose participation in the buy-sell [securities] transaction is a substantial factor in causing the transaction to take place." *Pinter*, 486 U.S. at 649–50; see *Cent. Bank*, 511 U.S. at 174–75, 179. Neither Section 11 nor Section 12 is enforceable by the Commission.

The PSLRA. In enacting the Private Securities Litigation Reform Act (PSLRA), Congress rejected proposals to overrule *Central Bank* and expand the scope of private civil liability under Section 10(b) to secondary actors. Instead, by enacting Section 20(e) of the 1934 Act, 15 U.S.C. § 78t(e), Congress expressly provided that aiders and abettors may be pursued in actions brought by the Commission. Thus, Congress gave the Commission, but *not* private plaintiffs, an express claim for conduct ("substantial assistance") by those who did not commit a primary violation of Section 10(b)—and required the Commission to pursue them as aiders and abettors, not primary violators.

More Recent Legislation. In considering the 2002 Sarbanes-Oxley Act, Congress again rejected proposals to allow private civil plaintiffs to sue secondary actors under Section 10(b). Specifically, the proposal was to give "the victims of fraud the right to sue those who aid issuers in misleading and defrauding the public." H.R. Rep. No. 107-414, at 53–54 (2002). That effort was rejected.

In the 2010 Dodd-Frank Act, Congress once more rejected similar provisions that were included in the original Senate version of the bill, in a stand-alone bill proposed in the Senate, and in a conference amendment proposed in the House. See S. 1551, 111th Cong. (2009); 156 Cong. Rec. S3569, S3618 (daily ed. May 12, 2010) (statement of Sen. Specter regarding Amendment No. 3776); *Discussion Draft of Restoring American Financial Stability Act of 2009* § 984 (Nov. 10, 2009); Ronald D. Orol, *Dodd Unveils Bank Reform Bill Without GOP Support*, MarketWatch, Nov. 10, 2009; Press Release, Rep. Maxine Waters, Waters Wins Big for Consumers, Homeowners, Minorities and Shareholders in Wall Street Reform and Consumer Protection Legislation (June 30, 2010). Instead, Congress expanded the Commission's authority to pursue and sanction aiders and abettors, see Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, tit. IX, § 929M 124 Stat. 1376, 1861–62 (2010), and ordered a GAO study of private aiding and abetting claims, see *id.* at, § 929Z 124 Stat. at 1871. The study, issued after *Janus*, noted the competing policy considerations and produced no recommendations. See GAO-11-664, *Securities Fraud Liability of Secondary Actors* (July 21, 2011).

These legislative decisions make "unsupportable" a reading of Section 10(b) and Rule 10b-5 that would transform a large number of aiders and abettors into

primary violators. See *Stoneridge*, 552 U.S. at 162. And yet the D.C. Circuit held that at least those aiders and abettors whose involvement with actionable misstatements "was not 'undisclosed' to investors" may be treated as primary violators. Pet. App. 24.

D. The D.C. Circuit's Interpretation Will Harm The Securities Markets.

Ratifying the bright-line "attribution is necessary" rule adopted in *Janus*, 564 U.S. at 147 n.11, would bring much-needed certainty to the securities laws and therefore to the securities markets. The Court has repeatedly stressed the need for unambiguous, readily administrable rules to govern and constrain securities-fraud litigation. Without these rules, the Court has admonished, private lawsuits can be employed "abusively to impose substantial costs on companies and individuals whose conduct conforms to the law." *Tellabs, Inc.* v. *Makor Issues & Rights, Ltd.*, 551 U.S. 308, 313 (2007). "[P]laintiffs with weak claims [can] extort settlements" from "innocent" companies that nevertheless fear "extensive discovery and the potential for uncertainty and disruption in a lawsuit." *Stoneridge*, 552 U.S. at 163; see also *Merrill Lynch, Pierce, Fenner & Smith Inc.* v. *Dabit*, 547 U.S. 71, 80–81 (2006).

These are not hypothetical concerns. In 2017, the number of federal securities class actions reached a record high—leapfrogging the previous record set in 2016. Press Release, Cornerstone Research, Securities Class Action Filings Reach Record High for Second Straight Year (Jan. 30, 2018), https://www.cornerstone.com/Publications/Press-Releases/Securities-Class-Action-Filings-Reach-Record-High. Although these suits are purportedly brought on behalf of shareholders, it is at least ironic that it is the shareholders who typically come out on the losing end of this phenome-

non. Since Congress enacted the PSLRA in 1995, securities class actions have wiped out over $701 billion in investment value and given shareholders only $90 billion. Inst. for Legal Reform, *Economic Consequences: The Real Costs of U.S. Securities Class Action Litigation* (Feb. 28, 2014), https://www.instituteforlegalreform.com/research/economic-consequences-the-real-costs-of-us-securities-class-action-litigation.

The direct cost of shareholder class actions, large as it is, is dwarfed by the indirect cost to the country's litigation-attracting public markets. Both SIFMA and the Chamber were involved in a recently issued report detailing the decline of public companies among American businesses. Ctr. for Capital Mkts. et al., *Expanding the On-Ramp: Recommendations to Help More Companies Go and Stay Public* (2018), https://www.centerforcapitalmarkets.com/wp-content/uploads/2018/04/IPO-Report_EXPANDING-THE-ON-RAMP.pdf. The sad fact is that fewer entrepreneurs are taking their companies public today, and when they do, they tend to do so later in their company's life cycle. At the same time, public companies increasingly are going private in part to avoid the litigation risks. The threat of abusive Section 10(b) and Rule 10b-5 litigation is one deterrent to going (and staying) public. That deterrent is largely grounded in a cause of action this Court created—the Court must ensure it remains appropriately narrow.

Of course, this is an action by the Commission, not a private suit. But this does not make the need for clarity any less acute. The Court's decisions delimiting categories of liability under Section 10(b) and Rule 10b-5 do not distinguish between Commission enforcement actions and civil suits. What the Court decides in this case will apply equally to suits brought by private plaintiffs. And in any event, clarity about scope of the

government's enforcement powers serves important ends as well. The investing public, regulated businesses, and the government officials charged with the prudent and lawful exercise of the powers conferred by the securities laws all stand to benefit from a decision that brings clarity by rejecting the Commission's effort to end-run *Janus* and undermine the well-defined liability rule established by that decision. See *Chiarella*, 445 U.S. at 235 n.20 ("a judicial holding that certain undefined activities 'generally are prohibited' by § 10(b) would raise questions whether either criminal or civil defendants would be given fair notice that they have engaged in illegal activity."); *FCC* v. *Fox Television Stations, Inc.*, 567 U.S. 239, 254 (2012) (agencies must give a "person of ordinary intelligence fair notice of what is prohibited" (quoting *United States* v. *Williams*, 553 U.S. 285, 304 (2008))).

II. THE D.C. CIRCUIT FAILED TO SEPARATELY DETERMINE WHETHER LORENZO COMMITTED A PUNISHABLE VIOLATION OF SECTION 17(a)(1).

Lorenzo also was held liable for violating Section 17(a)(1) of the Securities Act of 1933. Pet. App. 22, 77, 110. This Court should vacate this determination and remand to the D.C. Circuit for further proceedings for three reasons.

First, the D.C. Circuit's decision devoted little independent analysis to text, context, or history of Section 17(a)(1). Pet. App. 20–22; see also *id.* at 77 (Commission decision). The D.C. Circuit concluded that Lorenzo had violated Rule 10b-5(a) and (c), treated Section 17(a)(1) as a fellow traveler to those regulatory provisions, and thus concluded that Lorenzo must have violated Section 17(a)(1). For reasons shown above, however, the D.C. Circuit erred in concluding that Lorenzo violated Section 10(b) and Rule 10b-5,

and it is unclear from the lower court's opinion whether it would have sustained the Commission's finding that Lorenzo violated Section 17(a)(1) absent that error. Indeed, the D.C. Circuit never articulated any specific view of what conduct that statutory provision covers, stating only, at a high level, that Section 17(a)(1) "readily encompasses Lorenzo's actions." Pet. App. 22; see also *id.* at 33 ("Lorenzo's particular conduct . . . fits comfortably within the language of . . . Section[] . . . 17(a)(1)."). But of course, the D.C. Circuit made exactly the same observation—erroneously—about Rule 10b-5(a) and (c).

To be sure, the D.C. Circuit's treatment of Section 17(a)(1) as more or less equivalent to Rule 10b-5(a) and (c) is broadly consistent with the path taken by other lower courts. See, *e.g.*, *SEC* v. *Monarch Funding Corp.*, 192 F.3d 295, 308 (2d Cir. 1999) ("Essentially the same elements are required under Section 17(a)(1)–(3) in connection with the offer or sale of a security" as under Rule 10b-5."); *Landry* v. *All Am. Assurance Co.*, 688 F.2d 381, 386 (5th Cir. 1982). The lower courts have treated Section 17(a) and Rule 10b-5 similarly because the language of the two provisions is similar. In fact, the Rule's language was likely "derived in significant part" from Section 17(a). *Ernst*, 425 U.S. at 213 n.32.

But while the language is similar, it is not identical. For instance, Section 17(a) as a whole applies "*in* the offer or sale" of securities, 15 U.S.C. § 77q(a), whereas Section 10(b)'s applies to conduct "in connection with" covered transactions, *id.* § 78j(b). *Cf. United States* v. *Naftalin*, 441 U.S. 768, 773 n.4 (1979) (noting possible distinction between "in" and "in connection with"). Moreover, Section 17(a), unlike Rule 10b-5, is not governed by the limitations imposed by Section 10(b)'s "manipulative or "deceptive" language.

In part because of these differences—and in contrast to the D.C. Circuit's casual parallel construction—this Court has in the past interpreted Section 17(a) and Rule 10b-5 differently. For instance, the Court in *Aaron* concluded that a lesser state of mind was required by Sections 17(a)(2) and 17(a)(3) than by Rules 10b-5(b) and (c). See *Aaron*, 446 U.S. at 695–97. And the plaintiffs in *Santa Fe* argued that their broad reading of Rules 10b-5(a) and (c) was supported by the parallel text of Section 17(a)(1) and 17(a)(3). See Respondents' Brief at *9–15, *Santa Fe Indus., Inc.* v. *Green*, No. 75-1753, 1976 WL 181700 (U.S. Dec. 17, 1976). The Court, however, declined to tie Section 17(a)(1) and (a)(3) to Rule 10b-5 and resolved the case solely on the basis of Section 10(b).

In short, the Court has already held that Section 10(b) and Section 17(a) are not coterminous at least as regards the required mental state, and there are good reasons to think they may diverge in other ways as well. The Court accordingly should not adopt the D.C. Circuit's assumption that Section 17(a)(1) prohibits exactly the same sweep of conduct as Section 10(b) and Rule 10b-5(a) and (c).

Second, the posture of this case provides an additional reason for this Court to defer consideration of Section 17(a)(1), and in particular how it interacts with Sections 17(a)(2) and 17(a)(3). Section 17(a)(1) prohibits employing a "scheme" to defraud (a term found in Rule 10b-5(a) but not in Section 10(b)), but the Commission found only that "Lorenzo's role in producing and sending the emails constituted employing a deceptive 'device,' 'act,' or 'artifice to defraud' for purposes of liability under Section 10(b), Rule 10b-5(a) and (c), and Section 17(a)(1)"—pointedly omitting any reference to a "scheme." Pet. App. 77. The D.C. Circuit

did the same. *Id.* at 34 (Lorenzo "'engaged' in a fraudulent 'act' and 'employed' a fraudulent 'device' when, with knowledge of the statements' falsity and an intent to deceive, he sent the statements to potential investors carrying his stamp of approval as investment banking director."). At least one court of appeals has observed that a fraudulent scheme under Section 17(a)(1) may require "conduct beyond just misrepresentations or omissions" and thus set a higher bar than a Rule 10b-5(b) violation. *SEC* v. *Quan*, 817 F.3d 583, 589 (8th Cir. 2016) (quoting jury instructions). Given the absence of any fraudulent scheme finding in the record, this case does not present the Court with the opportunity to address the coverage of Section 17(a)(1) as a whole. A decision that implicates this critical provision without addressing its full contours would likely generate more heat than light and is in any event premature.

Third, as the Commission argued in opposition to Lorenzo's Petition, there is no substantial or developed Circuit split on the interpretation of Section 17(a)(1). BIO 17–18. Section 17(a) has in general received far less attention over the years than Section 10(b) and Rule 10b-5. Accordingly, the better course for this Court to follow is to remand to the D.C. Circuit for further proceedings regarding the Commission's Section 17(a)(1) charge. If the issue here is a recurring one, which is not clear, the Court can address Section 17(a) more fully in a later case.

CONCLUSION

For the foregoing reasons, the Court should vacate the D.C. Circuit's judgment and remand to that court for further proceedings with respect to Section 17(a)(1).

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In The Supreme Court of the United States

FRANCIS V. LORENZO,
Petitioner,

v.

SECURITIES AND EXCHANGE COMMISSION,
Respondent.

On Writ of Certiorari to the
United States Court of Appeals
for the District of Columbia Circuit

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INTEREST OF AMICI CURIAE

Amici curiae are law professors who teach and write about the federal securities laws.[1] They have an interest in the appropriate development and content of the laws governing liability for securities fraud in enforcement actions by the SEC and private civil actions for damages.

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[1] Pursuant to Rule 37.6 of the Rules of this Court, the undersigned hereby state that no counsel for a party wrote this brief in whole or in part, and no one other than *amici curiae* or their counsel contributed money to fund the preparation or submission of this brief. Pursuant to Rule 37.3(a) of the Rules of this Court, the parties have consented to the filing of this brief.

Virginia School of Law. He was Deputy General Counsel of the SEC and a partner in the securities enforcement practice of Wilmer Cutler Pickering Hale and Dorr LLP.

Karen E. Woody is Assistant Professor of Business Law & Ethics at the Kelley School of Business of Indiana University.

The views of the amici curiae expressed here do not necessarily reflect the views of the institutions with which they are or have been affiliated. The names of institutions are included for identification only.

SUMMARY OF ARGUMENT

The court below was mistaken in holding that the limitations in *Janus Capital Group, Inc. v. First Derivative Traders*, 564 U.S. 135 (2011), on primary liability for a misstatement do not apply to all parts of Section 17(a) of the Securities Act of 1933 (the "Securities Act"), 15 U.S.C. § 77q(a), and Rule 10b-5 under the Securities Exchange Act of 1934 (the "Exchange Act"), 17 CFR § 240.10b-5. The limitations on primary liability in both *Janus* and *Stoneridge Investment Partners, LLC v. Scientific-Atlanta*, Inc., 552 U.S. 148 (2008), apply to each subpart of those anti-fraud provisions and are essential to maintaining the dividing line established by Congress between primary liability and aiding and abetting under the federal securities laws.

Congress determined that an aider and abettor, that is, someone who did not engage in a primary violation, is a person who gives "substantial assistance" to a primary violation. If substantial assistance were enough for primary liability, as the

court below found, the distinction between a primary violation and aiding and abetting drawn by Congress in both the Securities Act and the Exchange Act would disappear. The difference between substantial assistance and conduct necessary to be a primary violator therefore is critical, yet the court below gave no consideration to the role of the "substantial assistance" language from the aiding and abetting statutes.

This Court's approaches in *Central Bank of Denver, NA v. First Interstate Bank of Denver, NA*, 511 U.S. 164 (1994), *Janus*, and *Stoneridge* also provide guidance on distinguishing between primary and aiding and abetting liability for securities fraud. Those decisions show that primary liability under Rule 10b-5 must be closely linked to a misstatement or misconduct that deceived a securities offeree, buyer, or seller. A primary violator is a person who has ultimate control and authority over that misconduct and who is separate and independent from other persons who may have participated in the fraud. The defendant in this case may well have given substantial assistance to the fraud committed by his superior, but he lacked the ultimate control and independence over the deception necessary to create primary fraud liability.

These principles apply to each subpart of Section 17(a) and Rule 10b-5. The language of Rule 10b-5 was derived nearly verbatim from Section 17(a). Some differences exist, but they do not affect the question in this case, which is the scope of primary liability under the two provisions. The identical language in the aiding and abetting statutes of the Securities Act and the Exchange Act supports the conclusion that the dividing line

between a primary violation of the anti-fraud provisions and aiding and abetting should be the same for both Section 17(a) and Rule 10b-5.

ARGUMENT

I. THE LINE BETWEEN PRIMARY LIABILITY AND AIDING AND ABETTING SHOULD BE THE SAME FOR ALL SUBPARTS OF RULE 10b-5 AND SECTION 17(a) AND SHOULD BE DERIVED FROM THE AIDING AND ABETTING STATUTES AND THIS COURT'S PRECEDENTS.

The question before the Court concerns the nature of the conduct sufficient for a primary violation of Section 17(a) of the Securities Act and Rule 10b-5 of the Exchange Act and the difference between primary liability and an aiding and abetting violation.[2] The question therefore is about the defendant's conduct, not the defendant's level of culpability.[3] The court below found that the *Janus* principles for determining primary liability for a

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[2] One of the amici curiae has written about several aspects of the issues now raised in this case. *See* Andrew N. Vollmer, *SEC Revanchism and the Expansion of Primary Liability Under Section 17(a) and Rule 10b-5*, 10 VA. L. & BUS. REV. 273 (2016).

[3] The rules on the level of a defendant's culpability or mental state are reasonably well settled. To be liable for a primary violation of Rule 10b-5 or Section 17(a)(1), a defendant must act with scienter. *See Aaron v. SEC*, 446 U.S. 680, 700 (1980); *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 (1976). To be liable for a primary violation of Section 17(a)(2)–(3), a defendant must act negligently or worse. *See Aaron*, 446 U.S. at 695–97. To be liable for aiding and abetting, a defendant must act knowingly or recklessly. *See* 15 U.S.C. §§ 77o(b), 78t(e).

misstatement under Rule 10b-5(b) (one subpart of the Rule) did not apply to distinguish primary liability from aiding and abetting for other subparts of Rule 10b-5 or Section 17(a)(1). The court failed to identify alternative principles or ground its decision in the structure and context of the Securities Act and the Exchange Act.

After *Central Bank* and Congress's addition the following year of aiding and abetting authority for the SEC but not private plaintiffs in Section 20(e) of the Exchange Act,[4] the difference between primary liability and aiding and abetting for a Rule 10b-5 violation took on critical importance. A plaintiff in a private securities action under Rule 10b-5, including a class action, may assert a claim for a primary violation but may not sue a person for aiding and abetting.

Both the SEC and private plaintiffs have been dissatisfied with that development. Private plaintiffs were most affected, and they responded to *Central Bank* and Section 20(e) by seeking to expand the scope of primary liability under Rule 10b-5 to reach solvent and deep-pocket defendants. Private plaintiffs started to assert that third parties who did not issue a misstatement to investors had

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[4] Pub. L. No. 104-67, § 104, 109 Stat. 737, 757 (1995) (codified at 15 U.S.C. § 78t(e)). In 2010, Congress granted the SEC a claim for aiding and abetting a violation of the Securities Act, the Investment Company Act, and the Investment Advisers Act. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, §§ 929M(a), 929N, 124 Stat. 1376, 1861, 1862 (2010) (adding Section 15(b) to the Securities Act, 15 U.S.C. § 77o(b), Section 48(b) to the Investment Company Act, 15 U.S.C. § 80a-47(b), and Section 209(f) to the Investment Advisers Act, 15 U.S.C. § 80b-9(f)).

nonetheless violated Rule 10b-5(a) and (c) by participating in a "scheme or artifice to defraud" and by engaging in a "course of business which operates . . . as a fraud or deceit" as a consequence of a business relationship with a primary violator that had issued a misstatement to investors. The SEC also broadened the concept of primary misconduct when asserting violations of Section 17(a) and Rule 10b-5, despite Congress's grant of authority to the Commission to sue aiders and abettors and assert other theories of secondary liability,[5] because the Commission prefers primary fraud charges.[6]

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[5] In addition to the general claim for aiding and abetting, the SEC may seek relief in an administrative proceeding against a person causing another person's violation. *See* Section 8A(a) of the Securities Act, 15 U.S.C. § 77h-1(a), and Section 21C(a) of the Exchange Act, 15 U.S.C. § 78u-3(a). The SEC may assert aiding and abetting and similar claims in an administrative proceeding to suspend or revoke the license of a regulated or associated person. *See, e.g.*, 15 U.S.C. §§ 78o(b)(4)(E), (b)(6)(A). Both the SEC and private plaintiffs may assert claims for control person liability under Section 15(a) of the Securities Act and Section 20(a) of the Exchange Act.

[6] The SEC's charging decisions in *Lorenzo* and an earlier case cited frequently in the SEC's *Lorenzo* decision, *Flannery*, are evidence that the SEC favors primary fraud violations. The SEC charged Lorenzo and Flannery only with primary violations. *See In the Matter of Gregg C. Lorenzo, Francis V. Lorenzo, and Charles Vista*, Exchange Act Release No. 68943, 2013 WL 587864, at *12 (Feb. 15, 2013) (Order Instituting Proceedings Against Greg C. Lorenzo); *In the Matter of John. P. Flannery*, Exchange Act Release No. 63018, 2013 WL 3826277, at *14 (Sept. 30, 2010) (Order Instituting Proceedings). The Commission also uses "scheme" liability to assert primary violations. *See, e.g.*, *SEC v. Goldstone*, 952 F. Supp. 2d 1060, 1133 (D.N.M. 2013); *SEC v. Kelly*, 817 F. Supp. 2d 340, 342 (S.D.N.Y. 2011).

Given the importance of the difference between primary fraud liability and aiding and abetting, this Court should use this case as an opportunity to clarify the line between the two prohibitions. If the lower courts and the SEC are allowed to smudge the line, this Court's decision in *Central Bank* and the aiding and abetting statutes would have no effect. As discussed in this brief, the Court's decisions in *Stoneridge* and *Janus* set down some markers on the boundary between primary and secondary liability under Rule 10b-5, but the court below and other lower courts have not fully accepted the Court's guidance.

Several sources of law help to explain the difference between a primary violation of Rule 10b-5 or Section 17(a) and aiding and abetting. They are the language of the statutes creating the aiding and abetting violation (Part A), the Court's decisions in *Stoneridge* and *Janus* (Part B), and the Court's precedents for giving a narrow scope to the elements of Rule 10b-5 (Part C). In Part D, we explain that the principles distinguishing primary misconduct from aiding and abetting should apply to all subparts of Rule 10b-5 and Section 17(a). Finally, in Part E, the brief argues that the aiding and abetting provisions, the overall structure and context of the statutes, and the Court's precedents rather than the language of Section 17(a) and Rule 10b-5—in isolation—should guide the Court's decision.

A. The substantial assistance element in the aiding and abetting statutes requires more significant conduct by a primary violator.

The language of the main aiding and abetting statutes, Section 15(b) of the Securities Act, 15 U.S.C. § 77o(b), and Section 20(e) of the Exchange Act, 15 U.S.C. § 78t(e), provides guidance on the difference between a primary violation and aiding and abetting. Congress said a key element of aiding and abetting is that the defendant must provide substantial assistance. Under the current version of Section 20(e), the SEC may bring an action against "any person that knowingly or recklessly provides substantial assistance to another person" that violated the Exchange Act or its regulations.[7]

If substantial assistance is required for aiding and abetting, primary liability must require more. If substantial assistance were enough for primary liability, no difference between a primary actor and an aider and abettor would exist. *Central Bank* and Congress's adoption of aiding and abetting provisions would have served no purpose. The statutory substantial assistance requirement tells us that a difference between primary liability and aiding and

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[7] Courts have applied the substantial assistance element. *See, e.g.*, *SEC v. Goble*, 682 F.3d 934, 947 (11th Cir. 2012) (finding that ordering false entries in records to allow a money transfer and signing the money transfer was substantial assistance); *SEC v. Fehn*, 97 F.3d 1276, 1282–84, 1287–88, 1293–96 (9th Cir. 1996) (finding that participation in the editing of information used to market securities was substantial assistance; also discussing adoption of aiding and abetting statute in the Exchange Act).

abetting must exist, and it must be meaningful and substantial.

One of the main flaws in the decision under review and the reasoning of other lower courts and the SEC is that they do not give appropriate weight to the congressional determination that an aider and abettor must provide substantial assistance to another who has violated the securities laws. That language and the very existence of the aiding and abetting statutes sets the boundaries of primary liability, yet the approach of many courts and the SEC is to pull and stretch the language of Section 17(a) and Rule 10b-5 to see if they can make it fit the conduct of the defendant in the case. These authorities view the line drawn in *Janus* as a nuisance to avoid, rather than a sensible reconciliation of the anti-fraud provisions with the statutes creating aiding and abetting liability.

That was the approach of the D.C. Circuit in this case. *Lorenzo v. SEC*, 872 F.3d 578, 589-95 (D.C. Cir. 2017) ("Lorenzo's conduct fits comfortably within the ordinary understanding of . . . the statutory and regulatory language" of Section 17(a) and Rule 10b-5), *cert. granted*, 138 S. Ct. 2650 (June 18, 2018). Nowhere did the court below explain how its interpretation of those provisions also fit with the substantial assistance language in the aiding and abetting statutes, which seems to apply more naturally to the defendant's conduct in this case. Moreover, the court below failed to explain why the limitations established in *Janus* were not appropriate to apply to all subparts of Section 17(a) and Rule 10b-5. Instead, the rationale of *Janus* was restricted to its facts. *Id.* at 590-91.

B. *Stoneridge* and *Janus* provide principles for identifying primary misconduct.

The Court granted certiorari in both *Stoneridge* and *Janus* to distinguish primary misconduct under Rule 10b-5 from aiding and abetting,[8] and both opinions did just that. *Stoneridge* involved allegations that suppliers to a publicly reporting company had violated Rule 10b-5. The company had made false statements to investors based on contracts with the suppliers. The Court limited primary liability by applying a proximate cause analysis to the reliance element of a private action and held that the suppliers were not liable when their dealings with the company were too remote and attenuated from the company's public misstatements. The company was the primary violator, and it made its own, independent decisions about disclosures to its investors, free from the control of the suppliers.[9]

Janus involved the potential liability of an investment adviser for allegedly false statements in the prospectus of a mutual fund. The Court limited primary liability under Rule 10b-5 to the person who makes a false statement. The maker is the person or entity with ultimate authority and control over the content of the statement and whether and how to communicate it. The funds, not the adviser, were the

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[8] *See Stoneridge*, 552 U.S. at 156; *Janus*, 564 U.S. at 141; *see also* Petition for Writ of Certiorari, *Stoneridge*, 552 U.S. 148 (No. 06-43), 2006 WL 1909677, at *i; Petition for Writ of Certiorari, *Janus*, 564 U.S. 135 (No. 09-525), 2009 WL 3614467, at *i.

[9] *Stoneridge*, 552 U.S. at 160–62, 166.

makers of the allegedly false statement. Although the investment adviser participated in the drafting of the funds' prospectuses and had significant influence over the funds, the funds and their boards were separate and independent and had final decision-making power over the contents of the prospectuses.[10]

Both *Stoneridge* and *Janus* stressed that limitations on the scope of Rule 10b-5 were needed to maintain a separation between primary liability and aiding and abetting. *Janus* reasoned that, for *Central Bank* to have any meaning, the Court must "draw a clean line between" those who are primarily liable and those who may not be pursued in private suits.[11] Allowing the SEC and private plaintiffs to do an end-run around the limits established in *Janus* would render that decision pointless.

The *Stoneridge* and *Janus* decisions show that primary liability under Rule 10b-5 must be closely linked to a misstatement or misconduct that deceived a securities offeree, buyer, or seller. A primary violator is a person with ultimate control and authority over that misconduct and is separate from and independent of other persons. Because the analysis distinguished between primary and secondary liability for the core concept of deception, the principles apply to each subpart of Section 17(a) and Rule 10b-5.

Stoneridge and *Janus* also show the gap between deceptive conduct for primary liability and

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[10] *Janus*, 564 U.S. at 142–43, 145–48.

[11] *Id.* at 143 & n.6; *see also Stoneridge*, 552 U.S. at 162–63.

substantial assistance for aiding and abetting. Assistance is not the commission of a deceptive act. The person who commits the violation does more than assist; he, she, or it must have final say over whether, how, and when a deceptive act occurs and must act independently of others. Assistance is help, support, aid, facilitation, or contribution to conduct that is undertaken by another. *Substantial* assistance is more than participation, a "but-for" cause, or a minor or trivial contribution. To be substantial, assistance must play a weighty, large, or material role in the violation.

C. The Court should apply a narrowing rule of construction.

This Court has held that, in construing primary liability under Rule 10b-5, courts should use a rule of construction that narrows the scope of liability. Because the private cause of action for violations of the Rule is judicially created, the Court concluded that it "must give 'narrow dimensions . . . to a right of action Congress did not authorize when it first enacted the statute and did not expand when it revisited the law.'"[12] The Court applied this view in *Janus* to an element of the Rule 10b-5 claim that both the SEC and private plaintiffs must prove, *i.e.*, the identification of the maker of a false statement. The limiting rule of construction therefore is not restricted to elements of a private claim only and should be applied in this case to control the reach of Rule 10b-5 including in SEC actions. In addition, because of the textual parallels between Rule 10b-5

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[12] *Janus*, 564 U.S. at 142 (quoting *Stoneridge*, 552 U.S. at 167); *see also Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 747–48, 749 (1975).

and Section 17(a) discussed below, that limiting rule should apply to both provisions equally.

The Court should not interpret Rule 10b-5 and Section 17(a) "flexibly" to effectuate their remedial purposes. Indeed, the Court has frequently rejected the use of that interpretive policy. Decades ago, the Court said that "generalized references to the remedial purposes" of the securities laws "will not justify reading a provision more broadly than its language and the statutory scheme reasonably permit."[13] The language, structure, and context of the securities laws are what matter. A flexible interpretive approach based on remedial purposes is empty of content, boundless, highly subjective, and inconsistent with the need to give a narrow scope to any Rule 10b-5 claim. The Court should explicitly renounce it.

D. The principles for primary liability under Rule 10b-5 also should apply to Section 17(a).

The text of Rule 10b-5 and the text of Section 17(a) are nearly identical. Some differences exist, but they do not affect the question in this case, which is the scope of primary liability under the two provisions. The principles for establishing primary liability should be the same for Rule 10b-5 and Section 17(a).

Rule 10b-5, which has evolved from a modest beginning to become the principal anti-fraud provision under the federal securities laws, is based on Section 17(a) of the Securities Act. As the drafter

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[13] *Aaron*, 446 U.S. at 695 (internal quotation marks omitted).

of the Rule, Milton Freeman, an Assistant Solicitor at the SEC, recalled: "I looked at Section 10(b) and I looked at Section 17, and I put them together, and the only discussion we had there was where 'in connection with the purchase or sale' should be, and we decided it should be at the end."[14] Given this provenance, it is appropriate to interpret the scope of primary liability under the two provisions the same.

Section 17(a) and Rule 10b-5 differ in a few ways, and those differences might be significant to the facts of an individual case, but the differences are not relevant to the issue raised by this case. One difference is that Section 17(a) applies to "the offer or sale of any securities," while Rule 10b-5 applies "in connection with the purchase or sale of any security."[15] This difference might account for some

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[14] Milton V. Freeman, *Administrative Procedures*, 22 BUS. LAW. 891, 922 (1967) (reporting Milton V. Freeman's remarks at the Conference on Codification of the Federal Securities Laws). Freeman and other members of the staff presented the draft to the Commissioners that morning or after lunch the same day, and the Commissioners unanimously approved the Rule. *Id.* *See also* Milton V. Freeman, *Foreword*, 61 FORDHAM L. REV. S1, S2–S3 (1993). This Court has noted the similarities. *See Ernst & Ernst*, 425 U.S. at 212 n.32.

[15] Other notable differences between Section 17(a) and Rule 10b-5 are the state of mind requirement and the availability of a private right of action, neither of which affects the question of the scope of primary misconduct covered by the two provisions. The Court held in *Aaron*, 446 U.S. at 697, that scienter is an element of a claim under Section 17(a)(1) but not Section 17(a)(2)–(3). Proof of scienter is a necessary element of a claim under Rule 10b-5. *Ernst & Ernst*, 425 U.S at 193 & n.12. The SEC has authority to assert a violation of either Section 17(a) or Rule 10b-5. A private plaintiff may bring a claim for a violation of Rule 10b-5 but, according to most courts of appeals, does not have a right of action under Section 17(a).

other differences in the language of Rule 10b-5(b) and Section 17(a)(2). Under Section 17(a)(2), a person may not "obtain money or property by means of" a misstatement, while Rule 10b-5(b) states that a person may not "make" a misstatement. The introductory language on obtaining money or property makes sense when the unlawful act is in the offer or sale of a security, which is the coverage of Section 17(a), but would not apply to an unlawful act in the purchase of a security. A more general scope was needed for Rule 10b-5, which applies to the purchase or sale of a security.[16]

The symmetry between Section 17(a) and Rule 10b-5 extends to the aiding and abetting provisions in the Securities Act and Exchange Act that supplement these anti-fraud prohibitions. The language of the aiding and abetting provision in the Exchange Act, Section 20(e), is identical to the aiding and abetting provision in Section 15(b) of the Securities Act. Given the use of identical language in these parallel securities laws, it is difficult to escape the conclusion that Congress intended that they should be read the same for purposes of determining primary liability.

The textual parallels between Section 17(a) and Rule 10b-5, on the one hand, and the aiding and abetting statutes in the Exchange Act and Securities

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See, e.g., Maldonado v. Dominguez, 137 F.3d 1, 6–8 (1st Cir 1998). For purposes of determining primary liability, the similarities in the language of the two provisions outweigh the absence of a judicially created private right of action under Section 17(a).

[16] *But see SEC v. Tambone*, 597 F.3d 436, 444–45 (1st Cir. 2010) (en banc).

Act, on the other, support the conclusion that the dividing line between a primary violation of the anti-fraud provisions and aiding and abetting should be the same for both Section 17(a) and Rule 10b-5. The cases that this Court has decided construing that dividing line for purposes of Rule 10b-5—*Central Bank*, *Stoneridge*, and *Janus*—should be equally relevant in construing the line between a primary violation under Section 17(a) and aiding and abetting under Section 15(b).

E. The aiding and abetting provisions, the overall structure and context of the statutes, and the Court's precedents rather than the language of Section 17(a) and Rule 10b-5—in isolation—should guide the Court's decision.

The Court's well-established practice when interpreting legal texts is to give effect to every clause and word of a statute or rule.[17] Various courts have engaged in that analysis of Section 17(a) and Rule 10b-5 as has the SEC.[18] Nevertheless, that exercise is not especially helpful when seeking limits to primary liability for the different subparts of

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[17] *See, e.g.*, *Corley v. United States*, 556 U.S. 303, 314 (2009); *Nat'l Ass'n Home Builders v. Defenders of Wildlife*, 551 U.S. 644, 669 (2007) (cautioning "against reading a text in a way that makes part of it redundant").

[18] *See, e.g.*, *SEC v. Tambone*, 550 F.3d 106, 120–23, 126–28 (1st Cir. 2008), reinstated in part by, 597 F.3d 436, 442–45 (1st Cir. 2010) (en banc); *SEC v. Stoker*, 865 F. Supp. 2d 457, 462–66 (S.D.N.Y. 2012); *In the Matter of John. P. Flannery and James D. Hopkins*, Exchange Act Release No. 3981, 2014 WL 7145625, at *11–18 (Dec. 15, 2014), vacated, *Flannery v. SEC*, 810 F.3d 1 (1st Cir. 2015).

Section 17(a) and Rule 10b-5. In this case, the relationship of the anti-fraud provisions to the aiding and abetting statutes, the overall statutory structure and context, and the Court's precedents are more important than the words of Section 17(a) and Rule 10b-5 plucked from context.

The words of the subparts do not set workable limits on primary liability. Moreover, with one exception, the subparts do not delineate different categories of misconduct. The key words for purposes of the question of primary liability are the verb forms: use, employ, obtain by means of, engage, and make. A person who violates the prohibition uses, employs, engages in, or makes the deception. Other words in the provisions, such as device, scheme, artifice, or act, do not assist in isolating the person who breaches a prohibition,[19] although they might be important in a specific case depending on the particular circumstances.

If the key words were construed without regard to statutory structure, traditional methods of interpreting statutes and rules might permit either narrow or broad constructions. For example, the first subpart of both Section 17(a) and Rule 10b-5 states that a person may not "employ" a device, scheme, or artifice to defraud. "Employ" means to "make use of, as an instrument, means, or material."[20] A person may "make use of" a deceptive act by being the person who made a final decision to

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[19] *But see In the Matter of Francis V. Lorenzo*, Exchange Act Release No. 74836, 2015 WL 1927763, at *11 (Apr. 29, 2015).

[20] WEBSTER'S NEW INT'L DICTIONARY 839, (2d ed. 1934).

have direct contact or communication with an investor or by being a person who arranged for the distribution of deceptive statements written, printed, and planned by another. The concept of employ could be a wide net or a fishhook. The SEC, in a now vacated administrative decision, interpreted Section 17(a)(1) and Rule 10b-5(a) broadly to reach the making of a false statement, the drafting or devising of a misstatement, or the orchestration of sham transactions to give the false appearance of business operations.[21] In this case, a majority of the D.C. Circuit panel held that Lorenzo employed a fraudulent device, but did not make an untrue statement, when he sent an email whose contents and recipients were ordered by his boss.[22] By construing "employ" broadly, while recognizing that it must construe "make" more narrowly, the lower court rendered this Court's construction of "make" in *Janus* irrelevant. Paying lip service to *Janus* is not enough, especially when the allegations in this case are about misstatements.

Similarly, this Court in *Janus* could have viewed the maker of a false statement either narrowly or broadly. The SEC and the Department of Justice contended that "make" should include creating, participating in the drafting, and providing false information that another person puts into a

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[21] *Flannery*, 2014 WL 7145625, at *12, *17.

[22] In a recent decision, the Second Circuit found that stock exchanges were exposed as primary violators on the theory they were co-participants in a market manipulation because they offered products and services to third parties that committed the alleged manipulative conduct. *City of Providence v. BATS Global Markets, Inc.*, 878 F.3d 36, 51 (2d Cir. 2017).

statement.[23] Justice Breyer in dissent argued that ordinary English usage did not impose unduly restrictive boundaries on the idea of making a statement.[24] Nonetheless, the Court rejected those contentions in concluding that the person with ultimate authority and control makes a statement. That interpretation was necessary to give effect to this Court's decision in *Central Bank* and Congress's response to that decision in enacting Section 20(e) of the Exchange Act. Considerations of statutory structure or other factors often demand a narrower construction than the maximum that the plain words will bear.[25]

In addition, the subparts of Section 17(a) and Rule 10b-5 do not indicate that they cover types of deception that are different in kind from each other. The first subpart of both provisions is worded generally to cover all types of securities fraud, including deceptive conduct. The second part of both provisions proscribes a particularized, but the most common, form of fraud—false and misleading statements of material fact. Misstatements are undoubtedly covered by the general prohibition on securities fraud, but they are nonetheless singled out for special mention in the second subpart. The third

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[23] *Janus*, 564 U.S. at 144–145, 148.

[24] *Janus*, 564 U.S. at 151 (Breyer, J., dissenting).

[25] For example, the Court imposed narrowing concepts on language in the bank fraud statute that resembles Section 17(a)(2) of the Securities Act. *Loughrin v. United States*, 134 S. Ct. 2384, 2393 (2014) (holding that the connection between a misrepresentation and the obtaining of bank property must be "more than oblique, indirect, and incidental"; "not every but-for cause will do").

part of both provisions refers to practices or courses of business that operate as a fraud or deceit. The difference between this wording and the first subpart on devices and schemes to defraud does not seem to reach different or broader types of conduct.[26] A practice that operates as a fraud is also a device to defraud.[27] Congress included considerable overlap among the three prongs of Section 17(a), which the SEC carried over to Rule 10b-5.

The overlap of the subparts of Section 17(a) and Rule 10b-5 is relevant because several lower courts have read *Janus* to apply only to allegations that a misstatement violated Rule 10b-5(b). Some courts, including the D.C. Circuit in this case, and the SEC have reached this conclusion with the goal of confining the effect of *Janus* to a narrow area and of expanding primary liability under other parts of Rule 10b-5 and Section 17(a).[28] Under this

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[26] The different wording does bear on the level of culpability needed for Section 17(a)(3). *See Aaron*, 446 U.S. at 696–97.

[27] *See Ernst & Ernst*, 425 U.S. at 199 n.20. In *United States v. Naftalin*, 441 U.S. 768, 774 (1979), the Court observed that each subpart of Section 17(a) proscribes a distinct category of misconduct covering additional kinds of illegalities, but it made the observation as a response to an argument that a phrase solely in Section 17(a)(3) should be read into all three subsections and without carefully examining the text of Section 17(a). *See also Aaron*, 446 U.S. at 697.

[28] *See Lorenzo*, 872 F.3d at 590–92; *SEC v. Monterosso*, 756 F.3d 1326, 1334 (11th Cir. 2014); *Lorenzo*, 2015 WL 1927763, at *10 ("because the language that a primary violator must 'make' a misstatement appears in only Rule 10b-5(b), the Division [of Enforcement] need not establish that a defendant 'made' a misstatement to establish liability under the other antifraud provisions").

interpretation, *Janus* has little application because making a material misstatement falls within the general category of schemes to defraud. Other courts have construed scheme liability in a way that gives *Janus* its full effect.[29]

Because the subparts of Section 17(a) and Rule 10b-5 overlap considerably, and because the differences do not separate primary misconduct from aiding and abetting, the different words of the subparts will not assist in resolving this case. Legal provisions often have redundancies, and courts will not always have a well-founded way to give separate effect to each and every word of connected provisions.[30] A delineation of the distinction between primary misconduct and aiding and abetting

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[29] *See Pub. Pension Fund Grp. v. KV Pharm. Co.*, 679 F.3d 972, 987 (8th Cir. 2012) (finding that a scheme liability claim must be based on conduct beyond misrepresentations or omissions actionable under Rule 10b-5(b)); *WPP Luxembourg Gamma Three Sarl v. Spot Runner, Inc.*, 655 F.3d 1039, 1057 (9th Cir. 2011) (stating that a "defendant may only be liable as part of a fraudulent scheme based upon misrepresentations and omissions under Rules 10b-5(a) or (c) when the scheme also encompasses conduct beyond those misrepresentations or omissions."); *In re DVI, Inc. Sec. Litig.*, 639 F.3d 623, 642–49 (3d Cir. 2011) (applying *Stoneridge* to deny class certification for scheme liability claims under Rule 10b-5(a) and (c) against an outside lawyer alleged to have participated in preparing a company's misleading public disclosures).

[30] ANTONIN SCALIA & BRYAN A. GARNER, READING LAW 176–77 (2012) ("sometimes drafters *do* repeat themselves and *do* include words that add nothing of substance"); Brett M. Kavanaugh, *Fixing Statutory Interpretation*, 129 HARV. L. REV. 2118, 2161–62 (2016) (book review) ("statutes often have redundancies, whether unintended or intended").

requires reference not just to text, but also to statutory structure, context, and precedent.

The precise language of Section 17(a) and Rule 10b-5 does not help separate a primary actor from an aider and abettor. Nor does the text of those provisions offer a reason to confine *Janus* to Rule 10b-5(b). Although the Court could dispose of this case with a rule preventing circumvention or evasion of *Janus* by making the principle underlying that decision applicable to any case involving a misstatement, the better approach would be to apply the principles from *Stoneridge* and *Janus* to all of the subparts of Section 17(a) and Rule 10b-5.

CONCLUSION

The Court should reverse and remand the case with instructions for the lower court and the SEC to apply the Court's limitations on the scope of primary liability for each of the subparts of Section 17(a) and Rule 10b-5.

Respectfully submitted,

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